UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

Case No. 18-23538-rdd

- x

In the Matter of:

SEARS HOLDINGS CORPORATION,

Debtor.

- x

Adv. Case No. 21-07011-rdd

- x

SEARS HOLDING CORPORATION,

Plaintiff,

v.

1055 HANOVER, LLC et al.,

Defendants.

- x

Adv. Case No. 20-06480-rdd

- x

KMART HOLDING CORPORATION et al.,

Plaintiff,

v.

WINNING RESOURCES LIMITED,

Defendant.

- x

United States Bankruptcy Court
300 Quarropas Street, Room 248
White Plains, NY 10601

May 25, 2021
10:15 AM

B E F O R E :
HON ROBERT D. DRAIN
U.S. BANKRUPTCY JUDGE

ECRO: UNKNOWN

HEARING re THE SEARS HOLDINGS CORPORATION HEARING WILL BE CONDUCTED USING ZOOM FOR GOVERNMENT VIDEO CONFERENCING. THOSE THAT REQUIRE ACTIVE PARTICIPANT or LISTEN ONLY ACCESS TO THE HEARING MUST EMAIL CHAMBERS AT RDD.CHAMBERS@NYSB.USCOURTS.GOV FOR ZOOM ACCESS CREDENTIALS.

HEARING re Notice of Agenda of Matters Scheduled for Hearing to be Conducted Through Zoom on May 25, 2021 at 10:00 a.m.

HEARING re Seventh Application of Weil, Gotshal & Manges LLP, as Attorneys for the Debtors, for Interim Allowance of Compensation for Professional Services Rendered and Reimbursement of Actual and Necessary Expenses Incurred from November 1, 2020 through and including February 28, 2021 for Weil, Gotshal & Manges LLP, Debtor's Attorney, period: 11/1/2020 to 2/28/2021, fee:$2,141,539.50, expenses: $143,450.70. (ECF #9416)

HEARING re Application for Interim Professional Compensation / Seventh Interim Fee Application of Prime Clerk LLC, as Administrative Agent to the Debtors, for Services Rendered and Reimbursement of Expenses for the period from November 1, 2020 through February 28, 2021 for Prime Clerk LLC, Other Professional, period: 11/1/2020 to 2/28/2021, fee:$3617.28, expenses: $5014.75. (ECF #9409)

HEARING re Seventh Application for Interim Professional Compensation of Akin Gump Strauss Hauer & Feld LLP as Counsel to the Official Committee of Unsecured Creditors for Allowance of Compensation for Services Rendered and Reimbursement of Expenses for the Period of November 1, 2020 through and including February 28, 2021 for Akin Gump Strauss Hauer & Feld LLP, Creditor Comm. Aty, period: 11/1/2020 to 2/28/2021, fee:$ 1,721,849.50, expenses: $2,262,474.82. (ECF #9412)

HEARING re Seventh Application for Interim Professional Compensation of FTI Consulting, Inc., Financial Advisor to the Official Committee of Unsecured Creditors of Sears Holdings Corporation, et al. for Interim Allowance of Compensation and Reimbursement of Expenses for the period: l/1/2020 to 2/28/2021, fee: $39,085.00, expenses: $0. filed by FTI CONSULTING, INC. (ECF #9415)

HEARING re Fourth Application for Interim Professional Compensation for Herrick, Feinstein LLP, Special Counsel, period: 11/1/2020 to 2/28/2021, fee:$565,994.5, expenses: $1,133.2. filed by Herrick, Feinstein LLP. (ECF #9410)

HEARING re Third Application for Interim Professional Compensation for Maritt Hock & Hamroff LLP as Special Conflicts Counsel to the Official Committee of Unsecured Creditors for Allowance of Compensation for James P Chou Maritt Hock & Hamroff LLP, Special Counsel, period: 11/1/2020 to 2/28/2021, fee:$29,686.00, expenses: $503.08. filed by James P Chou. (ECF #9408)

HEARING re Sixth Joint Application of Paul E. Harner, as Fee Examiner and Ballard Spahr LLP, as Counsel to the Fee Examiner, for Interim Allowance of Compensation for Professional Services Rendered and Reimbursement of Actual and Necessary Expenses Incurred from November 1, 2020 through February 28, 2021 for Fee Examiner, fee:$155,232.00, expenses: $700. 75. (ECF #9420)

HEARING re Debtors Twenty-Third Omnibus Objection to Proofs of Claim (No Liability Claims) (ECF #9284)

HEARING re Response to Debtors' Twenty-Third Omnibus Objection to Proofs of Claim (No Liability Claims)(RE: CLAIM NOS. 19509, 18092, 13404) (related document(s)9284) filed by James Edmond Smith. (ECF #9341)

HEARING re Motion to Amend/ Motion of Debtors to Amend Terms of Engagement of Preference Firms filed by Jacqueline Marcus on behalf of Sears Holdings Corporation (ECF #9469) Objection (related document(s)9469) filed by Joseph E. Sarachek on behalf of A&A HK Industrial, Esjay International Pvt. Ltd., Fuzhou Fushan Pneumatic Co., Ltd., Giza Spinning & Weaving Co., Helen Andrews Inc., Mien Co., Ltd., Mingle Fashion Limited, Samii Solutions, Shanghai Fochier, Vogue Tex (Pvt) Ltd., Wing Hing Shoes Factory Limited. (ECF #9490)

HEARING re Objection to Motion (related document(s)9469) filed by David H. Wander on behalf of Orient Craft Ltd. (ECF# 9492)

HEARING re Adversary proceeding: 21-07011-rdd Sears Holding Corporation v. I 055 Hanover, LLC et al Motion to Dismiss Adversary Proceeding (related document(s) 1)

HEARING re Adversary proceeding: 21-07011-rdd Sears Holding Corporation v. 1055 Hanover, LLC et al Opposition: Debtors' Opposition to Defendants' Motion to Dismiss (related document(s)4) filed by Jacqueline Marcus on behalf of Sears Holding Corporation. (ECF #9)

HEARING re Adversary proceeding: 20-06480-rdd Kmart Holding Corporation et al v. Winning Resources Limited Motion to Dismiss Adversary Proceeding filed by Alexander Tiktin on behalf of Winning Resources Limited. (ECF #11)

HEARING re Adversary proceeding: 20-06480-rdd Kmart Holding Corporation et al v. Winning Resources Limited Declaration of David H. Wander, Esq. (related document(s) 11) filed by Alexander Tiktin on behalf of Winning Resources Limited. (ECF #12)

HEARING re Adversary proceeding: 20-06480-rdd Kmart Holding Corporation et al v. Winning Resources Limited Declaration of Syed Mohi (related document(s) 11) filed by Alexander Tiktin on behalf of Winning Resources Limited. (ECF #13)

HEARING re Adversary proceeding: 20-06480-rdd Kmart Holding Corporation et al v. Winning Resources Limited Objection to Motion Plaintiff's Objection to Winning Resources Limited's Motion to Dismiss (related document(s) 11) filed by Steven J. Reisman on behalf of Kmart Holding Corporation, Sears, Roebuck and Co. (ECF #14)

Transcribed by: Sonya Ledanski Hyde

A P P E A R A N C E S :

WEIL, GOTSHAL & MANGES LLP
Attorneys for
767 Fifth Avenue
New York, NY 10153

BY: GARRETT FAIL
DOMINIC A. LITZ
JACQUELINE MARCUS

KATTEN MUCHIN ROSENMAN LLP
Attorneys for Kmart Holding Corporation
575 Madison Avenue
New York, NY 10022

BY: STEVEN REISMAN
TERENCE G. BANICH

ASK LLP
Attorneys for the Debtor
2600 Eagan Woods Drive, Suite 400
Saint Paul, MN 55121

BY: KARA CASTEEL

ALLEN MATKINS LECK GAMBLE MALLORY & NATSIS LLP
Attorneys for Landlords
Three Embarcadero Center, 12th Floor
San Francisco, CA 94111

BY: MICHAEL S. GREGER

ALSO PRESENT TELEPHONICALLY:

DAN MCELHINNEY, Stretto
PAUL E. HARNER, Examiner
JENNIFER CROZIER

P R O C E E D I N G S

THE COURT: Good morning, this is Judge Drain. We're here in re Sears Corporation, et al. on an omnibus day. I have the agenda for today's hearings. And I'm happy to go down the agenda, unless counsel for the Debtors wanted to make any opening remarks about the case generally.

MR. FAIL: Good morning, Your Honor. Garrett Fail, Weil Gotshal & Manges for the Debtors. Are you able to hear me all right?

THE COURT: Yes, fine.

MR. FAIL: Thank you. It's nice to see you. No statements about the case generally. One housekeeping matter. I think I see some folks on the Zoom that were subject to the Debtors' 23 omnibus objections to claims. As noted on the agenda, that matter is going forward today solely with respect to one party's claims. Mr. James Edmond Smith.

If other folks are on, I just wanted to let them know that the objection is not going forward with respect to their claims. They're welcome to watch the Zoom and watch the hearing, but if they have better uses of their time, I didn't want them to wait only to find out later.

THE COURT: Okay. Let me --

MR. FAIL: And that was as noticed, Your Honor, as noticed on the agenda and as folks were informed. I just

wanted to clean it up for housekeeping in case there are folks that thought that theirs was going forward today.

THE COURT: Okay. Let me make sure I -- everyone else understands that. So do you intend to submit an order granting the 23rd omnibus as to those parties who have not raised opposition to that omnibus objection, either --

MR. FAIL: That's happened already, Your Honor.

THE COURT: That's happened already.

MR. FAIL: Your Honor has granted on --

THE COURT: All right.

MR. FAIL: That's already happened.

THE COURT: So if someone --

MR. FAIL: But I think that there are a number of folks that have been carried from month-to-month as we've worked to resolve them.

THE COURT: Right. So if someone objected to that omnibus objection either formally or informally and that objection has not been resolved, it is not on for a hearing today. The only one that is on for a hearing is Mr. Smith.

MR. FAIL: Correct, Your Honor.

THE COURT: Okay. Very well. Thanks. And you'll notice the --

MR. FAIL: Okay, then we can --

THE COURT: -- you'll -- I'm sorry, you'll notice the hearings on the other ones in due course, if you're

unable to resolve them by agreement.

MR. FAIL: Correct, Your Honor.

THE COURT: Okay, all right. So then why don't we go back to the agenda?

MR. FAIL: Thanks very much, Your Honor. The first section on the agenda are fee applications. There are seven on for this hearing. All are uncontested. The applications are for in the order that they appear on the agenda or for Weil, Gotshal and Manges for Prime Clerk for Akin and Gump. For FTI Consulting, our clients (indiscernible) from Moritt Hock and for Mr. Harner as the fee examiner.

As has been the practice, we propose to submit (sound drops) omnibus order subject to anything that happens today, including the reservation of rights with respect to the fee examiner to challenge on a final basis as he continues to work with the various professionals.

THE COURT: Okay.

MR. FAIL: If Your Honor has any questions, I'm obviously happy to answer any.

THE COURT: All right. Now I see Mr. Harner on the Zoom screen. Even though there is this reservation of rights, has the fee examiner also reviewed the interim applications?

MR. HARNER: Your Honor, we're in various stages

of completion of review for various applications, including and through the 7th, we have not yet submitted preliminary reports on various of the 7th applications. We have largely submitted the preliminary reports rather on applications through the sixth interim period.

We're also in various stages of discussion with professionals about those and continue to hope to resolve them on a consensual basis without the involvement of the Court, but we have not submitted preliminary reports as of yet with prospective seventh applications. We are, however, satisfied with the reservation of rights, which paralleled that in the prior fee application orders with respect to the fee -- the ongoing review.

THE COURT: Okay. All right. As Mr. Fail noted, the applications are unopposed with that reservation of rights. Does anyone have anything further to say on them? All right. I have reviewed them.

And again, with the understanding that the fee examiner has been quite active in this case, and that his work is ongoing, including with respect to the time covered by these applications and all of his rights are reserved. I will grant the applications in the amounts sought. And again, subject to that reservation.

MR. FAIL: Thank you very much, Your Honor. Again, Garret Fail, Weil, Gotshal for the Debtors. The next

item on the agenda is the 23rd --

MR. HARNER: Your Honor, apologies, it's Paul Harner, the examiner. With that (sound drops) may I be excused?

THE COURT: Yes, that's fine. Thank you.

MR. HARNER: Thank you, Your Honor.

THE COURT: Okay.

MR. FAIL: For the next item, Your Honor, I'll hand the virtual podium over to my colleague Dominic Litz.

THE COURT: Okay.

MR. LITZ: Good morning, Your Honor. Dominic Litz from Weil, Gotshal, Manges on behalf of the Debtors. Can you hear me all right?

THE COURT: Yes, fine, thanks.

MR. LITZ: Good. Thank you, Your Honor. Your Honor, Item Number 8 is the Debtor's 23rd omnibus objection. And as Mr. Fail noted, we are going forward solely with respect to Mr. Smith's claims. That is -- the claim numbers are 8092, 13404 and 19509.

I'm going to collectively refer to those claims as the claim. Mr. Smith did file a response to the 23rd omnibus at ETF number 9341, and the Debtors filed a reply in support of the 23rd omnibus at ECF 9520. I do not see Mr. Smith in the video portion of the courtroom.

THE COURT: Right.

MR. LITZ: I don't know if he's appeared via phone?

THE COURT: Let me ask. Mr. Smith, are you on the phone? Again, it's James Edwin Smith. All right, he does not appear to be attending the hearing. He did receive notice of this hearing, though. And as you stated, filed an objection to the claim objection to his three filed claims. So you could go ahead, Mr. Litz.

MR. LITZ: Great. Thank you, Your Honor. Your Honor, the Debtors filed today 23rd omnibus objection back February of 2021, which objected to the claims on the basis that they failed to provide sufficient documentation support for the significant claim that Mr. Smith searched, which is in excess of $1.2 billion.

Mr. Smith has additionally failed to carry his burden to show that he is entitled to priority status, given the fact that the majority of his claims assert claims under wages for contribution as an employee of the Debtors.

Provide the Court with a little background, the three claims that Mr. Smith filed. Claim Number 8092 asserts an aggregate claim of $1.86 million, consisting of a secured claim for $874,000 and a claim for $836,000, keeping priority pursuant to Section 504, 50784, excuse me, Your Honor, of the Bankruptcy Code for hourly wages and a General Unsecured Claim of (sound drops) dollars.

We will lead to Claim Number 13404, Mr. Smith asserts $392,000 on a secured and Section 50784 basis, which appears to be a somewhat duplicative claim, 8092, and finally, Claim Number 19509 asserts a claim for over $1.2 billion third priority pursuant to Section 50785 of the Bankruptcy Code.

And Mr. Smith appears to assert all -- a small portion of that claim on a secured basis related to a letter (sound drops) First Trust of Illinois. The documentation and information provided with the claims falls well short of being able to support this significant claim.

Mr. Smith, with respect to Claim 8092 only submits a one-page questionnaire that seems to be prepared by Mr. Smith stating that he was an associate of the Debtors and had not received any benefits or wages since July of 2014. In Claim Number 13404, Mr. Smith appears to submit an alleged employment application, where he claims that he was hired as an investor by Sears on a salary basis at $74,000 annually.

And an additional draft (sound drops) addendum, which references Mr. Smith as the Director of the Debtor. Finally, Claim Number 19509 is supported by a portion of the one-page letter issuance of a letter of credit that speaks to have Mr. Smith, the beneficiary of $1.2 billion of a secured letter of credit. Your Honor, the Debtor has no --

THE COURT: There's no signature or any other evidence that this letter of credit is genuine, correct?

MR. LITZ: That is correct, Your Honor. There is an electronic signature. The inconsistencies among the documents are one of the many red flags that were pointed to the Debtors. It appears that an electronic signature of William K. Phelan is attached to various documents in different forms.

And one of the documents that shows a signature by Phelan, William K. and the other ones, it is William K. Phelan, who is a former Director or employee of Sears. However, it is the Debtor's -- the Debtor's information believes that, you know, Mr. Phelan did not sign his name back essentially with Phelan, K. Williams.

Going back to the Debtor's review of the books and records, there is no information or record of Mr. Smith being an employee of any capacity, whether it was (sound drops). It's unclear what an investor for the Debtors would appear to do, and there is no record of Mr. Smith being a Director of the Debtors.

As the Court is aware, Mr. Smith bears the burden to prove that he is entitled to priority status of these claims. And it is clear through the papers and the documentation that he has failed to do so. As the Debtors wrote in their papers, there are many inconsistencies from

when Mr. Smith was an alleged hire, the title or position that Mr. Smith allegedly held with the Debtors, and whether he was an hourly or salaried employee.

Your Honor, the Debtors will request that the Court disallow and expunge all three claims in their entirety on the basis that they lack sufficient documentation information, and that Mr. Smith failed to establish (sound drops).

However, if the Court -- to the extent the Court disagrees and the Debtors -- and that the Debtors have to evaluate the claim a little bit further, at a minimum, the Debtors would request that the third claim be disallowed in full because there's no property of estate that secures a $1.2 billion letter of credit.

And to the extent that the Court believed that Mr. Smith is entitled to and allowed wage claim, the Debtors would note that it should be capped at $12,850, which is the cap of Section 50784 at the time the Debtors filed it. I'm happy to answer any questions Your Honor may have.

THE COURT: No, I don't have any questions. I will grant the objection to these three claims in full. They're truly bizarre documents that have no support whatsoever other than what appear to be forgeries. The Debtors have asserted that Mr. Smith had no employment relationship with them. He is not refuting that with any

evidence other than his conclusory statements, which are self-contradictory.

He's asserted claims based on purported stock investments, and otherwise, really can't explain the claim at all. In addition, he's asserted priority claims, again, in a situation where it does not appear that he was an employee of the Debtors ever. Those claims obviously due exceed the statutory cap for priority in any event.

Similarly, he asserted a claim on a secured basis, attaching a facially and credible purportedly heretical standby letter of credit for in excess of $1.2 billion. The whole claim is -- all three claims, that is, are simply in-credible. And the Claimant hasn't carried his burden of proof on any aspect of them. So you can email me what are disallowing the three claims in full.

MR. LITZ: Great. Thank you, Your Honor. I'll submit an order to Chambers, and I will cede the virtual podium to my colleague, Ms. Jacqueline Marcus.

THE COURT: Okay, thank you.

MS. MARCUS: Good morning, Your Honor. Jacqueline Marcus from Weil, Gotshal on behalf of the Debtors. Item Number 9 on today's agenda, a motion of the Debtors to amend the terms of engagement of preference firms, Docket Number 9469.

As laid out in the motion, back in June of 2019,

the Debtors engaged a trio of law firms -- ASK LLP, Active and Recovery Services, now Stretto, and Katten Muchin Rosenman LLP, which we refer to in the motion as the preference firms, to prosecute the Debtor's avoidance actions, which constituted one of their largest assets.

At that time, we described the terms of the engagement support and other parties in interest, specifically the terms of the contingent fees that were to be paid were set forth in the respective engagement letters. Based upon their experience between April 2019 and December 2020, the preference firms realize that due to the incompleteness or inaccuracy of the information which they had been provided, the contingent fee schedule they had negotiated did not fairly compensate them for the work they were doing.

As noted in the motion, there were three primary issues. The number of executory contracts that would be assumed and assigned to transform as part of the sale transaction, the amount of the cash in advance payments that were made by the Debtors prior to the commencement date, and the lack of information to substantiate certain payments made by treasury wire.

The preference firms approached the Debtors and requested a modification of the contingent fee schedule, as contemplated by each of the engagement letters. On behalf

of the Debtors, M3 and the restructuring committee of the Debtor's Board of Directors, reviewed the proposed modified terms and negotiated with the preference firms to actually reduce the fees that had been requested.

The repricing proposal described in the motion sets forth the result of those negotiations. The key terms of the repricing proposal are as follows -- an incremental contingent fee that will enable the preference firms to recoup some of what they had expected to earn -- excuse me -- if certain thresholds were met, the potential for a one-time $500,000 payment, if gross recoveries exceed a certain designated threshold on July 31, 2022, and importantly, a step down in the revised commission rates of 50 basis points, if the thresholds are not as achieved by certain target dates.

If approved by the Court, the new commission rates will take effect as of January 1st, 2021. The repricing proposal has been discussed and vetted with the administrative creditor's representative and the Creditor's Committee, who has indicated in the motion to not oppose the relief requested.

In addition, before it was filed, the motion was provided to the Office of the US Trustee, and the US Trustee authorized us to represent to the Court that it does not object for the requested relief.

The Debtors believe that the revised terms fairly compensate the preference firms for the work they are doing, and provide an incentive for them to maximize the value realized on the preference claims, and to do so on an expedited time frame.

Two objections to the motion were filed by administrative expense creditors. One group of Creditors represented by Mr. Sarachek, who opted into the administrative claims consent program or did not opt out. And Orient Craft Limited, which opted out of the administrative claims consent program.

Neither of the objections relates to the reasonableness of the compensation to be provided to the preference firms under the revising proposal. Instead, they both complain about the extent to which their respective administrative expense claims have received distributions to date, but that is not the issue before the Court today.

It's not the responsibility of the preference firms to ensure that administrative creditors, whether opt-in, non-opt out or opt out will be paid in full. The question before the Court is whether to approve the Debtor's business judgment that modifying the compensation as set forth in the repricing proposal is in the best interest of the Debtors and their constituents, and provides a reasonable rate of compensation for the preference firms.

The Debtors believe that the answer to both of these questions is yes, and we urge you to grant the motion. Unless Your Honor has any further questions, I would cede the virtually podium to Terence Banich of Katten.

MR. BANICH: Good morning, Your Honor. Terence Banich of --

THE COURT: I did have --

MR. BANICH: Oh, excuse me.

THE COURT: I did have some questions. I'm not sure why we're hearing from the three firms as opposed to just the objectors first. But my questions really go to points that I think are separate from the objectors, which is the standard by which I need to review this.

Each of these firms -- well, first of all, my question is, which firms are we talking about? Because there is a tie-in to the Acumen firm. And it's not clear to me how that works in relation to this compensation package as proposed.

Secondly, the firms, including Acumen, were retained under 328(a), as far as their compensation was concerned, which has a high standard for altering compensation terms.

And then, finally, I'm just not -- it's not clear to me whether that standard is satisfied here. And then, but finally, if it is, I guess I have a question as to what

is a reasonable rate for a replacement firm at this point, if the firms are not willing to work on the terms that they had originally negotiated.

But maybe the first question I would have is, which firms are covered by this and how does it relate to the Acumen fees?

MS. MARCUS: So I think I understand your question, Your Honor. This applies to all three firms, which amongst themselves have an arrangement, and maybe Mr. Banich can help me on this, in terms of the sharing of the compensation. But Stretto basically just stands in Acumen's shoes and the revised terms would apply to all three firms. I don't know if that answers your question.

THE COURT: So I mean, each one had a different percentage. I mean, Acumen and Stretto had a different percentage, for example.

MS. MARCUS: Right, and --

THE COURT: And the other ones, they're all now on a uniform percentage.

MS. MARCUS: I think it's -- the way I would describe it is it's all in the mix. I'm not sure with respect to whether certain of the firms are getting more in certain circumstances. But the way we've presented it is the blended basis at the end of the day for all three firms working together.

THE COURT: But how does that -- I'm just not sure how one would measure that. I mean, ultimately, if I grant this, there will be fee applications. And in fact, the fee applications aren't normal fee applications. They just show what is recovered by the firm.

And I just -- I mean, are they the same ratios as before, with Acumen? I -- it's just not clear to me that -- how this -- I guess what you're saying to me is this is an -- these are aggregate commissions or aggregate contingency fees.

And as between any of, you know, ASK or Katten or Stretto, they're going to allocate them as they allocate them. It doesn't really matter as far as the Debtors are concerned?

MS. MARCUS: It actually doesn't matter as far as the Debtors are concerned, as long as the aggregate compensation to be provided is reasonable and appropriate. I don't know, and we have representatives of all three firms on the Zoom, if any of them want to speak to that.

THE COURT: Well, I mean, each of them separately --

MS. MARCUS: But that's not changing.

THE COURT: Each of them --

MS. MARCUS: I think the important thing -- I'm sorry.

THE COURT: Okay. Each of them separately submits a report, which in essence is under their retention orders, a request for compensation. I don't even know if the other ones get notice of that. And I, you know, I review it. And if the math works out, I'll grant it.

But I don't want one of the other ones coming back and said, oh, you over authorized ASK, for example. And under our sharing arrangement, we should get some of that. That's a concern I have. I understand the Debtor's point. We want to -- they're just paying an aggregate sum, an aggregate contingency fee.

But as among the various firms, I -- you know, before, there were specific percentages for each firm. And they would represent that they were following those percentages. It's just not clear to me now if that's how they're going to make their representation as to what they themselves are owed as among the three of them.

MR. REISMAN: Well, Your Honor -- Jackie -- sorry, apologies, Jackie, to talk over you. Your Honor, Steven Reisman of Katten. We will not be back before Your Honor with an issue between Katten and Stretto. You have my word. I am telling you that. We will never be before you to deal with the issue.

We will work it out. Mr. McElhinney is on the line. Basically ask that they're commissioned and Katten

and Stretto get the same amount that ASK gets for the same dollars, right, on what -- if they collect $5 million and it's 10 percent, they get $500,000.

If we collect $5 million, 10 percent, you get $500,000. And we divide it out based upon an agreement that we will disclose and share with the Court and state that that is -- assuming Your Honor grants the relief.

I assure you, (sound drops) that we literally -- the last thing you'll have to deal with will be an issue. Mr. McElhinney from Stretto is on the line. We've been -- we've managed to -- are working together. We're all really working, all three of us are working together to maximize the value here and spending.

You know, without getting into numbers or anything, literally millions and millions and millions of dollars in fees from (sound drops) to fully prosecute these actions and maximize the recovery to the benefit of the estate.

I don't want to get into the argument on the motion. Mr. Banich will handle that, but I want an answer to Your Honor's questions to the extent that's a sufficient answer. And if you have any follow-up I'm happy to respond.

THE COURT: Okay. Well, I mean, under the existing engagement agreements, the compensation is different for each firm, right? It's a different percent as

far as the contingency fees are concerned.

MR. REISMAN: Each share with Stretto at the same level as when asked for the recovered -- Dan, will you care to answer?

MR. MCELHINNEY: Your Honor, Dan McElhinney on behalf of Stretto. I'm going to clarify first that Stretto is not a law firm. We were retained as an advisory.

THE COURT: Right.

MR. MCELHINNEY: An advisory firm to provide data analysis of the advisory services. And as Mr. Reisman suggested suggested, we are teamed with Katten. So the fees -- ASK has one set of -- it has a fee that is mirrored by the combination of fees in our retention applications between Katten and Acumen.

So if you add up in each level, the percentages for Katten and Acumen, they will equal at that level ASK's percentage. So they are mirroring. It's just that you look at Katten and Acumen with specific, you know, their percentages -- the split between Katten and Acumen is defined in our retention applications.

It's not intended to change by virtue of this application. So whatever those percentages are will remain the same, or the split, the average split as between the two firms could stay the same. And ultimately, they will mirror exactly the percentage that ASK will (sound drops) for their

services.

THE COURT: Okay. So in other words, the AS -- I'm sorry. The ASK Stretto arrangement and the Katten Stretto arrangement as far as the allocable share to -- between the law firm and Stretto in each case doesn't change as far as allocable share. It just changes as far as the base.

MR. MCELHINNEY: ASK -- it's -- ASK is essentially on its own. They do the legal and the data advisory portion. So for example, in tier two, for matters that are cases where complaints had been filed, under the existing proposal or under the existing pricing, ASK would receive 17 percent.

For all of their settlements, they get a commission of 17 percent. On that same level, to -- they're 17 percent applicable to Katten and Acumen that's with 10 percent to Katten, seven percent to Acumen. That's essentially how the split works. So Stretto only works with Katten on their matters. We provide the data advisory component. And Katten provides the legal services.

THE COURT: So again, as far as Acumen and Stretto are concerned, the split percentage doesn't change, just the base amount of the aggregate commission changes?

MR. MCELHINNEY: Right. The commission to be applied changes, but the split -- what we received versus

what Katten receives is the same. The percentage is the same. It won't change. It won't increase any of the percentage.

THE COURT: And is that the same for ASK and Acumen?

MR. MCELHINNEY: Again, ASK doesn't work on -- we basically split the entire portfolio so that Stretto and Acumen have their and ASK have their cases. Stretto does not work or provide --

THE COURT: Okay.

MR. MCELHINNEY: -- for ASK.

THE COURT: All right. Fine.

MS. MARCUS: Your Honor, if your second question had to do with the standard in 328A --

THE COURT: Right.

MS. MARCUS: -- for modifying compensation -- excuse me. I guess I'll start off by noting that the engagement letters themselves have the possibility of modifying the commission rates, upon Court approval.

But, I read 328A and the standard of improvident when granted more as the situation where the Court has approved compensation and is then going to reduce the compensation, as opposed to a modification going forward of the terms.

THE COURT: It goes both ways. If someone

asks for more, the standard goes both ways. Reductions and increases.

MS. MARCUS: I guess you could say that the compensation was improvident -- it's a heard word, but improvident when granted, because based on the facts as they turned out to be -- the compensation that had been agreed to turned out to be below a market rate of compensation for the services. And that's the reason that the preference firms made the request, and that's the reason that the Debtors took the time to really review the numbers and the performance, and negotiated, at arm's length with the firms over the modification.

THE COURT: Well, again, it's, it's improvident in light of developments not capable of being anticipated at the time of fixing of such terms and conditions. So it's more than -- it, you know, it turns out to be a bad deal. It has to have been incapable of anticipating that it would be a bad deal.

MS. MARCUS: I'm sure when the terms were negotiated that each of the firms made certain assumptions, and provided some -- I would imagine, some amount of cushion in terms of what the likely recoveries would be. But given the magnitude of the cases and the complexity of this failed transaction, then the monumental task of assuming and assigning contracts and all of that stuff, I think -- reason

what we (indiscernible) could differ as whether it could have been anticipated that numbers would be that far off.

MR. STEINFELD: Your Honor, this is Joseph Steinfeld, can you hear me?

THE COURT: Yes.

MR. STEINFELD: Okay. Hi. I'm lead attorney for ASK. I will be and as was represented, our firm is basically divided half the cases and we're a law firm, as Your Honor knows, and we do the analysis as well. So our fees are completely set the same way. They're not going to change other than the percentages may slightly alter from what we have right now.

But I did want to address the Court's concern about the process when we did this case. I was intimately aware of, and I was involved in that. And one of the big issues for us was we were told, we were given a list of assumed contracts, and we did cull those out of our analysis. But then after we were engaged and the process with Commensic Transform Halco had the ability, unbeknownst to us at the time, to go in and for a period of time, to assume additional contracts. And that had a dramatic effect on a lot of -- of the larger cases, a lot of the larger recoveries. So that did effect one thing.

The other thing is, we were told that the records of the Debtor were such that we were going to be

able to get the invoicing and the payment detail from Treasury Checks, which were wires, and again, that was a process that dragged on for months. I mean, almost a year with some difficulty from Transform Halco in giving us the information we wanted.

And subsequently, when we did receive some of that information, did reduce the entire portfolio. Dan McElhinney would know this, but I think it was a rather significant percentage rate, 30, 40, 50 percent of the actual portfolio was reduced.

So those, for some of the items that we were facing that we were unhappy at the time that we did the case. So I'd just address the Court to say those are the basic issues that -- I think we've plead those also, but maybe there wasn't quite as much detail in the papers.

THE COURT: Okay.

MS. MARCUS: I think your last question, Your Honor, was what it will cost to get another series of firms or a firm in here --

THE COURT: Right. Well, before you answer that one, I don't -- there's no statement in this motion as to what the aggregate increase really is over what the current arrangement is. What is the -- what is the increase in the percentage for the tiers involved? That's T I E R S, for the court reporter's benefit. As against the existing

percentage?

MS. MARCUS: So as you've noted, Your Honor, and it is a very complex formula, in that M3 has sent an analysis of what the blended rate would be under this same proposal -- excuse me, under the existing arrangement and the modified proposal.

THE COURT: Right.

MS. MARCUS: Under the existing arrangement, the blended rate should come out to be approximately 14 percent. Under the modified proposal, it could be as much as 17.8 percent, if that one time $500,000 payment was achieved, or as little as 15.5 percent, if alternatively, the stepdown happens because the time thresholds haven't been met.

So I think it's fair to say that it's a little more than 3 percent of a change. And the, the basis for that is there was some effort to enable the preference firms to recover or recoup what they thought they would have gotten if the data had been correct at the time. So if they're able to satisfy those thresholds, they'll recoup a little bit of what they were, in effect, were giving up because of the incompleteness or inaccuracy of the data.

THE COURT: Okay. And is this -- is there $500,000 for each firm? Each of the two firms? The law firms?

MS. MARCUS: No, Your Honor, it's to be shared.

MR. STEINFELD: It's an aggregate.

MS. MARCUS: Yes, it's to be split.

THE COURT: Okay. All right. And then you were going to answer my question which is, what due diligence have the Debtors done with regard to the potential replacement compensation for a different firm?

MS. MARCUS: So to be frank, Your Honor, I don't think -- we haven't gone down that road to see what the replacement compensation would be. And part of the reason, or the main reason for that is that this was not posed to the Debtors as change or compensation or we're quitting. I don't think any of the firms has said that. There hasn't been any discussion that I'm aware of that they've said that. It was more in the nature of we don't think we're being fairly compensated so make the adjustment.

I do know that the people who were responsible for negotiating the terms, initially, are very well versed in what the market is for these kinds of arrangements and were well aware of that when we were negotiating a repricing proposal, but I don't think they've gone out to seek other firms to replace these firms. But frankly, I would expect partly given the, you know, the knowledge that we have now, and partly given the stage that

we are in the cases, that any other firm who would come in to replace these firms would probably be charging a lot more. But that's pure speculation on my part.

THE COURT: How does this compensation relate to an hourly rate? An average hourly rate?

MR. STEINFELD: Your Honor, without -- Your Honor, without getting into -- without getting into specifics, right? And you can understand the reason for that. I think you can, based upon your prior experience. This will be a -- this will not fully compensate us for our hourly rates. This will not. And it will be below. I can't tell you how it's going to end up. Right now, the gap is wide. The hope is that this will somewhat narrow that gape as we had no -- we believed the information that we got, and we did not think that Sears, you know, but and it's no fault. I don't want to try to put blame on anybody, but we did this quickly.

We did this as accurately as we could, and we came up with the numbers that we came up with, and had the numbers been what we had expected, we would not be coming back. Right? Because the number went up as we went on. Right?

When you cut a major number off of the, you know, nine figure number, off of the -- not the, we'll just leave it at that. But off of the numbers, it has a dramatic

impact on the ultimate, which I've already -- and the percentages that we would earn. So that's why -- and we're not, I would never do that. That's not Katten, ASK, Stretto, never. We're not saying, Your Honor, you know, either do this or -- we would never put you in that position and we would never do that to a client that we are privileged to have the pleasure of representing. It's just that the information, we had no possibility of any way realizing that after the fact, that all of these contracts that (indiscernible) were going to so -- and that all this information that we relied on being one direction turned out to be, sorry, it's another direction.

THE COURT: Okay.

MR. MCELHINNEY: I don't want to steal Mr. Banage's thunder in any way, and I don't know if he has anything further to add that regard, and apologies for jumping in here. Just wanted to try to help out with the interest to the questions. And if now, I'd be happy to answer any further questions.

Your Honor, I turn the podium over to the next -- the next speaker.

THE COURT: Okay. Well, why don't I hear from the objectors.

MR. WANDER: Good morning, Your Honor, can you hear me okay?

THE COURT: Yes, good morning.

MR. WANDER: David Wander of David Roth Hatrens Hitron, Counsel for Oregon Craft. It's very good to see you, Judge, and it's good to see everybody else.

Your Honor, I can't overstate the seriousness of this application, and the implications, and no one really wants to or seems to be addressing that. When I read the Debtor's motion, and I read what the preference firms are alleging, it appears to be making out a claim for fraudulent inducement. And I found that shocking and I'm going to tell you why.

Last night, I went over the transcript from the confirmation hearing. And I read it from the beginning to the end, skipping over a few portions that didn't really involve this. And first, it you're -- and I'm sure, Your Honor, will recall, I cross-examined the Debtor's witnesses. And the testimony on the purported preference recoveries, the projected preference recoveries was tremendously significant to the Court's decision to confirm the plan. And I first cross-examined, Brian Griffin, on the preference matters. And his testimony was that the Debtor's projected preference recoveries of $100 million.

I pressed him on that, and I asked him, and this is at page 70 of the transcript on October 3rd, 2019. And he said it depends on when -- what the preference firms

are able to bring in, in the next three months. So I pressed him, what was his best guess of the preference recoveries by the end of the year? That would have been two weeks in October, November, and December. And his testimony, at page 70 was by the end of the year, the recoveries would be between $15 and $20 million. Now, let's keep in mind this is before Covid-19 pandemic.

I then pressed him about 2020. And his testimony was that the projected recovery by the end of 2020 was $60 million. Again, that would include months before the Covid-19 pandemic resulted in global shutdown. And the balance $20 million would be in 2021. And he testified about discussions with the preference firms, and that's on page 71.

And, Your Honor, I've been asked about the discussions with preference firms. That's on page 80. And Debtor's counsel, Mr. Ganinder, talked about conversations with preference firms on page 80. And -- I'm sorry, on page 86. And that they were relying, in part, on the preference firms. And Mr. Ganinder said on page 88, no administrative claim shortfall was projected.

Next was Mr. Murphy. Mr. Murphy said the preference firms were still conducting diligence relating to perfect potential preference recoveries. And that testimony starts a little after page 134. Mr. Shrop then stated at

page 145, he referred to the restructuring committee. He said, "they're pressing the preference firms. You know, making sure that they're going to be those complaint's filed … in the very near term." He goes on to say "we think that we can go effective within a few months. As early as, you know, within a few months." And then he says on page 164, "I hit the preference actions, which, you know, we're hopeful that those will be even larger than what we put the estimates on."

Counsel for the committee, Mr. Dublin, starting at page 205. He talked about we've had recent conversations with counsel for the states that are pursuing the preference actions. We expect upwards of 200 complaints to be filed before the end of the month. That process is ongoing.

Then at the end of the testimony, Your Honor, and I had some colloquy, and Your Honor, pressed me. You asked regarding the Debtor's plan, the why is this a visionary skim? That's what you asked me. And I responded, and I said, and this is at page 239, and it goes onto page 240. I said, it will be years for money to come in based on preference recoveries. I repeated myself. "So it'll be years for the preference recoveries and the funds to come in to pay administrative claim." I then said, so we have a plan that may be effective in three years.

Now, Your Honor said, at page 248, as far as -- "as far as I'm concerned, I have uncontroverted evidence that there is a more than reasonable likelihood that there will be at least $100 million in preference recoveries." Then the confirmation hearing was adjourned.

As Your Honor, may recall at that time, I was doing the cross-examine. I was primarily representing Pro Global, and in between the confirmation hearings we settled our claim. And that was put on the record at the beginning of the adjourned hearing that I believe was on October 7th.

Though I wasn't in a position, really, to speak further, and then at the end on page 180 of the transcript, when Your Honor, was explaining why you were confirming the plan, you said, "I believe that the likelihood of satisfying section 1129A9 in the relatively near term, i.e. in a matter of months, is established."

But now, the firms that have been involved since April. May, June, July, August, September -- about six months of working on the preference matters, no one said anything at the confirmation hearing about these Transform issues, about incomplete documentation. With over $150 million, I believe at that time, in professional fees, on these matters. Now the preferenced firms say to Your Honor, based in the debtor's motion, "Before the documentation and information necessary to accurately address the Court's

actions was available". They agreed to the contingency arrangement before they had accurate information. And the Debtor's Motion goes on to say, according to the Debtor's the preference firms now allege "that a significant portion of the documentation and information provided to the preference firms, prior to the engagement, turned out to be inaccurate or incomplete, requiring additional time, money, and resources to prosecute the preference -- the avoidance actions."

According to the Debtor's motion, the preference firms now allege "that had they been fully apprised of the number of contracts that had been assumed by the Debtors and aside to Transform, which necessarily reduced potential preference claims". Judge, we are now here, and I submit that the information that was given to Your Honor, to get this plan confirmed was false or misleading.

THE COURT: Well, that's not the issue before me today, and it's really unfair to bring it up today with references to a transcript that no one has gone back to look at, including myself. So I'll say --

MR. WANDER: I think you should just --

THE COURT: -- let's focus on the standard for this motion which --

MR. WANDER: -- yes, I would --

THE COURT: -- some of your remarks are addressing, but other than that it's not -- it's not before me.

MR. WANDER: I wanted --

THE COURT: So we're not going to go down that road.

MR. WANDER: Okay. I wanted just to set that up as part of the foundation for the objection. I'm saying that these firms, who are among the most experienced firms in the business of prosecuting preference actions, had whatever information available to them that Your Honor, had in confirming the plan. And Oregon Craft opted out, so every dollar that goes to the professional is one less dollar that is available for the plan to become effective.

Now, when I read the motion, I was saying to myself, if they don't get this increase, does that mean they won't work diligently? I frankly have never heard of that. That a lawyer retained to represent a debtor, Chapter 11, that if they're not going to get paid as much as they thought they would, they then won't work as hard? They won't be incentive? Oregon Craft has no objection to the estates paying these firms whatever they want to after the plan goes effective and Oregon Craft is paid it's undisputed administrative claim, I think that the focus, going forward in this case should be less concern about how much the

professionals are going to be making, what we're recouping, and should be concerned about the creditors. The administrative creditors being paid. Thank you, Your Honor.

THE COURT: Okay.

MR. SAROCHEK: Your Honor, Joe Sarochek from Sarochek Law Firm on behalf of Mead and various other administrative creditors. To address the standard, we are questioning the Debtor's business judgement, real hard, myself and Mr. Wander. We're in a situation now where -- and I want to preface by saying, these are quality firms that we're dealing with. Ms. Gressman's firm, the other firms, we've had a lot of interaction with them. They're very competent. They're quality firms. We're not questioning their competency in any way, shape, form.

We don't believe they are the issue here. The issue here is that there's an $80 million hole, and this debtor, and I've reviewed all of the fee applications, to date, last night, and this Debtor has generated over $240 million of fees without expenses, that have been paid. And we're focused on a 3 percent change in preference firms that, to date, have generated $16 million? We are questioning Debtor's business judgement. I want to be really, really clear. And we think there is cause, at this time, Your Honor, for the appointment of a trustee in this case as an alternative.

THE COURT: Again, that is not before me either.

MR. SAROCHEK: I understand it's not before you, Judge, but you are being asked to modify a fee arrangement when we're in a situation, 18 months subsequent to confirmation and the Debtor is focused on a cut where the patient is bleeding to death. I mean, this is equivalent to trying to solve the Covid crisis without finding a vaccine. What, what is the Debtor's business judgement in focusing on this? As opposed to focusing on resolving the ESL litigation, which is the only source of funds. It's crystal clear. The only source of potential funds to make this plan go effective. And for us to focus on the preference issue, at this time, really we are questioning their business judgement, Your Honor. And we don't believe that you should take this up at this time. And we do believe that there are other, more pressing issues. Thank you.

THE COURT: All right. Well, I -- I guess I understand you and your client's frustration, but I've never heard of a situation where it's a requirement for a debtor to carry a particular burden of proof on a particular motion that they explain all of the other things that they're doing or not doing in a case. The two are just not combined. So I would have thought that if you were objecting on the Debtor's business judgement, it would be their business

judgement with respect to this particular proposed agreement, as opposed to something else.

You and your clients, certainly have their rights to seek other forms of relief, but I guess, I don't -- I don't really stand -- understand the objection of this particular motion on that basis. On the other hand, I do have a concern that this request, although it might be supported by business judgement to incentivize further the firms to accelerate their recoveries, which is what at least Mr. Sarochek is wanting, although he doesn't believe, and I tend to agree with him at this point, that the recoveries won't be sufficient even if accelerated to warrant the plan going effective.

I still have a problem with the 328A point. I just don't -- I don't have enough of a record here to show that these circumstances were not unanticipatable at the time that these compensation agreement were entered into. Including the fact Transform had the ability to assume contracts and make cure payments, which in effect takes the matter out of the preference category.

So I think without more, I can't approve this. It's just not within 328A. Which clearly does work both ways. There are times when firms get windfalls. There are times, on the other hand when their investment doesn't turn out. And I just don't have enough of a record today to

establish that the exception to that provision would apply here.

MR. MCELHINNEY: Your Honor, if I may make a suggestion, right? We've heard your ruling, right. So unless we think that we can meet that standard, right, and make a supplementary little submission in that regard, we'll pull the motion. Right. So it's either to be, right, we're not going to make the motion, or we're going to supplement the record. So in the regard -- and I'm not looking to cut off Mr. Sarochek and Mr. Wander, great respect to both of them, and as professionals to preserve their right on whatever supplemental submission was made as to the standard in that regard to satisfy 328.

That's just one point I wanted to suggest to Your Honor, if I could. The other is, is that I want to be clear to Mr. Wander, none of these three firms that I would speak, without having spoken to them, because I have spoken to them enough. We are going to act diligently. We have acted diligently. We are, you know, working very hard. That the polite say to say it. Right. It is the thought that went to my head, but it is the polite way to say it. We are working very hard to try and make this a success. And appreciate Mr. Sarochek's comments in that regard. He recognizing the work that we're doing, and we will continue to do that, Your Honor. It's not -- I understand the point

of sometimes it turns out that, you know, but this, this was like -- this is a big number. Right. So what I would like to say is before we get into it, there are sensitivities in regards to certain things. If we could either we'll withdraw it, or we will put in a supplemental sufficient and we stand to adjourn.

THE COURT: Okay.

MS. MARCUS: And Your Honor, Your Honor, on behalf --

MR. MCELHINNEY: Sorry, Jackie, it's not my, oh I'm sorry, Ms. Marcus --

MS. MARCUS: That part of what I was going to say, but what we'll do is, if you wouldn't mind adjourning this matter and we'll consult with the preference firms and the restructuring committee, and figure out what we're going to do, and provide notice and act accordingly.

I would like to just respond on a couple of little point, and, Your Honor, I know you noted that they're irrelevant. This is not the forum for relitigating confirmation, and likewise, no request has been made for the appointment of a trustee. And I think it's completely inappropriate, and I won't even respond top that request. It's just totally off based in this context.

THE COURT: Okay. I will adjourn this to the next omnibus date and again see whether at that point the

firms and the debtors want to go ahead with the relief or would rather, would extend withdraw it. And again, I want to be clear, the standard that I'm looking at this under, is, is not the business standard judgement. It's the 328A standard. As far as business judgement, the Debtors may well have made their case except with regard to the $500,000 because I don't understand what triggers that. And that is probably about the same concerns about telegraphing too much to the defendants in the preference actions. But it's -- it just says recovery support and agreed upon threshold, without really, you know, fleshing that out.

And that does seem to have a disproportionate effect on the aggregate estimated change from the estimated contingency fee as it would exist today, as Ms. Marcus represented at least, almost three points change. But the thing to focus on, again, is whether the information available to the firms at the time that I approved the certentions, was enough so that it was anticipatable that they'd be in this position today. Or alternatively, whether there was something that was not available to them that really means that this was improvident when entered into, because it wasn't anticipatable. And frankly, I think the risk that Transform is going to assume contracts, is something that you wouldn't have known about because that's part of the deal. But that's something that you can submit

additional evidence on if you want to.

MR. STEINFELD: Your Honor, can you hear me? Joseph Steinfeld. I just wanted to raise one issue and I expect a ruling shortly, but I don't want to leave an impression that we have not worked exceedingly hard in this case and will --

THE COURT: I -- I don't have that impression --

MR. STEINFELD: Okay. Good.

THE COURT: -- and I frankly don't think either of the objectors rise that objection.

MR. STEINFELD: But I also --

THE COURT: When they referenced the size of fees, it's really not the fees of the --

MR. STEINFELD: It's not our fees, I know.

THE COURT: -- special counsel -- preference counsel.

MR. STEINFELD: But I do want to also point out, and I think Mr. Reesman said it as well, regardless of what happens, whether we ever come back to the court or doesn't get approved, we're going to work just as hard, and I just don't want the implication that somehow in the motion we need this in order to work harder, I disavow fairly great.

THE COURT: I don't have any doubt in that --

MR. STEINFELD: Thank you.

THE COURT: -- frankly, Ms. Marcus' remarks confirmed that because the Debtors really didn't either. That really wasn't their focus --

MR. STEINFELD: Very good.

THE COURT: -- their focus was on what they --

MR. STEINFELD: Thank you, Your Honor.

THE COURT: -- believed was fair. And unfortunately, 328A is not necessarily a model of fairness. It's fairness as of the time of retention, but not, not later. You know, these, these issues about the course of the case and the payment of administrative expense creditors come up at every conference we've had. At every omnibus day, and they've come up today too. I trust that the parties are working on them in a way to try to go effective.

It doesn't appear to me that the best way to reach a settlement with over 30 sophisticated defendants in a mega lawsuit, is to tell them we really need some money right now. So I'm just not sure that's really the optimal way to go, Mr. Sarochek, but on the other hand, I think that they probably should be focusing on a way to share the burden of the administrative expenses in order to go effective.

MS. MARCUS: Your Honor, we are looking -- we

are looking at that, and as you know, the Debtors don't control the ESL litigation, pursuant to the confirmation order. But we're working with all parties to try to expedite things and move this case alone.

THE COURT: All right. Okay.

MS. MARCUS: The next item on the calendar, Your Honor, we're moving into the advisory proceedings, and the next item on the calendar is number ten, the Motion to Dismiss. I'm not quite sure which counsel is handling that part, but the two landlords.

MR. DEVAIN: This is Robert Devain, (indiscernible) on behalf of landlords 1055 --

THE COURT: You're -- you're --

MR. DEVAIN: Can you hear me?

THE COURT: -- almost too much. You're coming through really loudly.

MR. DEVAIN: Okay. I will turn down my -- speak more softly then, if that's okay.

THE COURT: Yes, that's better,

MR. DEVAIN: Again, Robert Devain, Kelly Drye and Warren, on behalf of landlords and defendants in this case, and (indiscernible) and for LLC, and (indiscernible) Boulevard, LLC., Your Honor. (Indiscernible) and my colleague Mike Greger and Alan Mackets, I would like to clear up a bit of housekeeping.

Mr. Greger and I, and (indiscernible) were admitted Pro hoc in the main proceeding back in November of 2018. We filed Pro Hoc's for them this morning in this atmosphere and those fees have been paid, but not entered, but just with your permission be allowed to have Mr. Greger on this motion from Alan Mackets.

THE COURT: That's fine.

MR. DEVAIN: Thank you very much. With that, I will cede the podium on our motion to dismiss to Mike Greger.

THE COURT: Okay. And just so the parties know, I've reviewed the complaint, the motion, the objection to the motion, the reply, and the exhibits, which are the two leases, which are obviously referenced in the complaint, and therefore something that I can review as part of the motion to dismiss. So you should assume I have that background here.

MR. GREGER: Thank you, Your Honor, Michael Greger of Alan Matkins (inaudible) on behalf of 1055 Hanover, LLC and 1 Imson Park Boulevard, LLC. Your Honor, the landlords seek dismissal under rule 12-B-6 of Debtors adversary complaint, which asserts a single cause of action for turn over under Section 542 of the code.

As set forth, more fully, in Landlord's motion under subtle bankruptcy law, a turnover action, under

Section 542 only applies to property that belongs to the bankruptcy estate. A debtor cannot use the turnover provisions of Section 542 to liquidate contract disputes or demand assets whose title is in dispute. The existence of a bonafide dispute regarding an asset or a debt prohibits the turnover action under 542.

As set forth more fully in our motion and our reply papers, Your Honor, the Landlords submit the Debtor's complaint should be dismissed with prejudice as it fails to state a claim under Rule 12-B-6. Because the Debtors have failed to establish any valid basis, or at least have failed to establish that the prepaid rent they're seeking to turn over is not subject to a bonafide dispute.

Your Honor, the fact in this matter are really not --

THE COURT: Well, can I interrupt you on that point?

MR. GREGER: Yes, Your Honor.

THE COURT: If I granted their complaint on that basis -- I'm sorry, if I granted the motion on that basis, the Debtors would be free to then seek a declaratory judgment, I'm assuming, that this is -- the prepaid rent is property of the estate, correct? Or that there's an obligation to turn it over -- not turn it over, to -- it's free from either a set off of a couvment rider or a -- if

it's a debt?

MR. GREGER: Your Honor, I -- in terms of what theories the Debtors could pursue if the Court were to deny a turnover under 542, what we know definitively, is the Debtors have no right to assert any affirmative rights under the contract. They rejected the underlying leases and have no, no rights any more to reap the benefits of the leases they rejected. That's the effective rejection.

Whether or not they have any additional rights under state law, we don't think so. We think under the fact of this case, as set forth more fully, in motion, the prepaid rent became nonrefundable upon payment except as otherwise provided in the leases. The leases here are very clear, Your Honor, with respect to the right to recover prepaid rent. They're defined in both leases in paragraphs 36.

Paragraph 36 both state that upon execution of the leases, the Debtors were to prepay months 7 through 18 of the leases. The Debtors admit, in their complaint, that they made the prepayments. And Your Honor, we submit under state law, the effect of that language is very clear. And of course, state law is what controls this issue, because the United States Supreme Court, long ago in Butner vs. the United States, in the Seminole decision made very clear that state law define property rights here.

THE COURT: Except where the bankruptcy code provides otherwise, which was the rest of the quote that everyone leaves out from Butner.

MR. GREGER: But the bankruptcy code does not provide otherwise here, Your Honor, with respect to the prepaid rent. And when we look at paragraph 18, it uses very -- I'm sorry, paragraph 36 of the leases, it uses very specific language. The landlords -- the Debtor's "prepaid rent, due under the lease for the months 7 through 18 of the term. The term prepaid rent has a specific meaning, under state law, as Landlord's briefed in their motion and replay, under state common law, prepaid rent under a lease becomes Landlord's property, under state common law, and may be retained upon a tenant's default or breach, an absence of a provision of the lease that requires a refund.

In determining whether or not prepaid rent falls within this common law rule, the 5th Circuit interpreting Florida law, which is relevant here, and of course, this was back in 1962, before the 5th Circuit split into the 5th and the 11th Circuit, so it was the controlling Circuit, controlling Florida District Courts and Bankruptcy Courts at the time, ruled that in determining what constitutes prepaid rent, the Courts must "look to the language of the lease". In it's iconic the lease language had -- the language is a simple language that provides for a

deposit that was to be made upon execution of the lease that was going to be applied against future rent.

The court in looking at that language said proper construction of the lease is that the lease provided for an advance payment of rent, which fell within the state common law rule for the State of Florida. And that rule, as we already discussed provides that once paid, the rent becomes nonrefundable, and in absence of the landlord's default. And of course there was no landlord default here.

The enforcement of the parties written agreement as written, weaves its way in many cases in both Florida and Pennsylvania. The Florida Supreme Court has, on multiple occasions, weighed in on what the effect of prepaid rent is under state law. And for example, in the casino amusement case from the 1930's the Florida Supreme Court found that a simple provision the lease provided for a $25,000 payment, that "shall be credited as rent for the last year of this lease", was prepaid rent that fell within the common law rule.

In Householder Black in the 1950's the Florida Supreme Court, again, weighed in and said where a lease had a provision that said that a deposit was made and will be applied against the third year of the term payable in advance on execution of the lease. The prepaid rent fell within the common law rule.

Similar to Florida, Pennsylvania courts have a long history of enforcing parties agreements as written, particularly in the commercial context where sophisticated parties are involved. Pennsylvania courts have specifically recognized the rights of parties to negotiate for prepaid rent. Moreover, that right exists, notwithstanding any potential forfeiture that occur -- can occur.

Pennsylvania courts have also articulated a standard that in the breach of contract context, where a party has advanced money and then stopped short of performance, that party will not be permitted to recover back the advance paid. Given the strong common law favoring freedom of contract in Florida and Pennsylvania, courts will uphold the parties to their contracts, as written.

Here, Your Honor, we have sophisticated commercial parties that were both represented by counsel. They intentionally chose to define the payments at issue as prepaid rent. The language used is unambiguous and has clear meaning under both Pennsylvania and Florida law. The parties written agreement in paragraph 36, the prepaid rent falls squarely within the common law rule and becomes nonrefundable, except as otherwise provided in the lease.

That leads us under what terms the leases permit refundability. And Your Honor, the leases do provide a very limited right to refund in Section 36, but that right

is limited to where the landlords are in default. Where a condemnation event has occurred, or where the landlords exercise their right of early termination, provided in paragraphs 3 of the leases.

None of those provisions that are all -- are at all applicable here. Instead we have the Debtors reject the lease, as we all know under 365G of the bankruptcy code constitutes a default, a breach, and in the breach context, Your Honor, the leases don't provide the Debtor with any rights to refund. So we fall up under the state common law rule that the prepaid rent belongs to the Landlords and is nonrefundable to the Debtor as a matter of law.

THE COURT: I've read the Florida cases. It's not clear to me that that rule applies in Pennsylvania. You're saying that it should apply because it generally applies throughout the country?

MR. GREGER: Yes, Your Honor. And more specifically, we, we believe that the -- and I'm trying to remember the name of the decision, I believe it's the Hutchinson vs. Sunbeam decision from the Pennsylvania Supreme Court in 1986, in footnote 4, the Court said very specifically in Pennsylvania, that parties are free to bargain for minimum advance rental. So I think --

THE COURT: Well, I understand that, but that just begs the question. I mean, I understand that

Pennsylvania like, I think all states, says that the parties are free to bargain for what the contract will say. The issue here is that there is a unstated term on the contract which is what happens to the prepaid rent in the event of the Debtor default. It doesn't say that the Landlord can keep the money, it doesn't say that the Debtor can keep the money. It just is silent. So the general principal from Pennsylvania law doesn't really address that specific situation when a contract is signed. You're asking me to read into a provision consistent with common law around the country.

MR. GREGER: Actually, Your Honor, we don't believe we're asking you to read into a provision. We believe that the contract clearly provides that the prepaid rent was due upon execution of the leases. And once paid, the parties have the right to dictate in the commercial real property lease when rent is due. The parties agreed that the rent was due upon execution, and it was paid upon execution.

Thereafter, the contract merely provided a provision that how it would be applied, assuming the Debtors weren't otherwise in default. It provided, assuming the Debtors, weren't in default, it would be applied against the monthly rent for the months of 7 through 18 as and when due.

THE COURT: Well, actually, it actually says otherwise due during the months of 7 through 18. That's where the use of the term due is provide -- is used.

MR. GREGER: Right. That's correct.

THE COURT: It just says the Debtor shall provide the amount in advance, but it's with respect to the amount otherwise due, and then it says how it shall be applied.

MR. GREGER: Assuming the Debtors aren't in default.

THE COURT: I understand. I understand.

MR. GREGER: Right. Where they're in default, they don't get that application, nor do they get the prepaid rent back, which was paid --

THE COURT: Well, it doesn't say that. I guess that's, that's my point. I doesn't really say what happens when they are in default. Now, there is a --

MR. GREGER: But the --

THE COURT: -- I think it's fair to say there are, there are plenty of Florida cases that say you don't have -- and the debtor doesn't have an interest in that -- an ownership interest in that rent at that point. I understand that proposition. I'm just saying I don't see that dealt with yet under Pennsylvania law.

MR. GREGER: And what we submit, Your Honor,

is the state law of the common law, virtually all of the states that we've seen, as we've submitted the ALR article that deals with these issues. And we've identified numerous states in our brief, but it seems to be the vast majority, if not exclusive that virtually all states under the common law, provide for a concept of prepaid rent that becomes nonrefundable, absence a default.

THE COURT: Okay.

MR. GREGER: And we submit that Pennsylvania would follow a similar rule.

THE COURT: Okay.

MR. GREGER: The Debtors -- the Debtors have no real response to the state law, other than to interject a whole host of arguments trying to argue that somehow the prepaid rent they admitted paid to the Landlord, actually wasn't the Landlords. For example, the Debtors make the argument what the prepaid rent was actually in what amounted to a trust. I'm not really certain what is meant in the complaint, when they say it amounted to the trust, because there is no such concept under the law. Are they referring to an express trust? Because there is no express trust here, as we cited in our reply brief. In order to create an express trust, you have to have an expressed intent to create a trust.

Here, the lease doesn't say the money is put

in a trust. It has no prohibitions against comingling, it has no requirements against segregation. It has no -- imposes no responsibilities on the landlord, it imposes no duties at all, other than provided in Section 36, the limited right of refund, and the right of the Debtor to have it applied against the rent, assuming it's not then in default. Other than that, it's entirely silent. And we submit, Your Honor, without any such provisions in a lease, it can come no where near establishing an express trust, under the law.

With respect of a constructive trust, the Debtors due argue that there is some form of unjust enrichment here, but as we cited under both very clear and dispositive Pennsylvania and Florida law, the doctrine of unjust enrichments is inapplicable when the relationship between the parties is founded upon a written agreement or an expressed contract, regardless of how harsh the provisions of such a contract may seem in light of subsequent happenings.

There's just no basis, therefore, to have a constructive trust here. They next argue that maybe this is a bailment, but then of course a bailment is a specific contract where the parties agree to the delivery of personality, for the accomplishment of the purpose in the contract. That also requires an expressed intent to create

a bailment, and there's no provision in this contract for the creation of a bailment. There's not even an obligation to comingle. Or to segregate the funds, or to return the same funds, so there can't be a bailment.

The debtors then respond with a very bizarre arguments, as far as I can tell, that, that what really is happening here is that we have some property interest in the prepaid rent, and because we reject the leases, we "terminated" the Landlord's right to rent and their obligation to pay rent, and because there's nothing to apply the prepaid rent against, it has to be refunded based upon the power provided under 365 of the code, Your Honor.

It's extinguishment theory, however, was expressly refutiated and rejected by the Supreme Court Mission Product. Where the Supreme Court expressly determined that the rejection does not terminate and agreement or strip a counter party of its rights. In fact, quoting the language from the Supreme Court, the Supreme Court said a rejection does not terminate the contract. When it occurs, the debtor and the counter party do not go back to their prepetition positions. Instead, the counterparty would change the rights it has received under the agreement, as after a breach, so too after rejection. Those rights survive. In other words, Your Honor, rejection doesn't terminate any of our rights to the prepaid rent.

All of the rights under the contract and the rights under state law, survive. So the debtor's argument that somehow 365 is an affirmative avoidance action that allows it to recover the prepaid rent, is just simply false, Your Honor. We submit.

The last arguments we deal with, Your Honor, is that even if we are incorrect on a concept that state law makes prepaid rent nonrefundable, landlords still have rights of recoupments. And recoupments rights arise as an affirmative defense to a payment obligation. When the party -- when the obligation arise out of the same agreement. You know the debtor's response to recoupment is that should apply here because that would frustrate priority schemes of the code. Well, that's what the courts have determined that recoupment does. Recoupment isn't subject to the priority schemes of the code. It's a state law defense that where obligations -- mutual obligations arise under the same agreement. The obligations effectively cancel each other. And we asset, Your Honor, there's no better case for recoupment than here. That the lease and the prepaid rent, all of the obligations arose under the same agreement. The obligation to pay prepaid rent is set off or recouped against the obligation to pay the same rent. So for example, the debtors reap the benefit of the prepaid rent for months 7 through 12 of this lease by not paying their

365-D3 obligations by recouping it, literally here. And now when the flip side of the situation arises and the landlords want to recoup months 8 through 13, post rejection,the Debtors argue that recoupment's not available. I mean, very inconsistent positions the Debtor is taking here with respect to recoupment. They themselves --

THE COURT: Well, one could argue you're doing the flip side of that. I mean, which is natural because whenever you're opponent takes a position, you would oppose it. So --

MR. GREGER: Right, Your Honor. But they received --

THE COURT: But if -- but if the amount is --

MR. GREGER: -- they took the --

THE COURT: -- due prepetition, how could it be applied to a post-petition obligation given a mutuality --

MR. GREGER: What is --

THE COURT: -- the mutuality requirement?

MR. GREGER: Well, recoupment --

THE COURT: If the prepaid rent is, in fact, due prepetition --

MR. GREGER: Yeah. So --

THE COURT: -- how could it be applied to a post-petition obligation?

MR. GREGER: With -- with respect to recoupment,

Your Honor, the obligation mutuality doesn't apply. You can cross --

THE COURT: Well, I know. I know.

MR. GREGER: -- petition date.

THE COURT: But that's -- that's an issue that --

MR. GREGER: So, now you're talking --

THE COURT: -- that's an issue that the parties have barely touched upon, the recoupment issue. And frankly, since this is a motion to dismiss a complaint that seeks turnover, which goes back to my first question, I'm not sure it's really proper for me to decide that issue in this context, as opposed to, as you've requested -- and I think is a legitimate request -- although here, I'm not sure who's arguing this on the Debtor's counsel's side, them on it -- say that the turnover complaint is dismissed without prejudice because there is a bona fide dispute here as to ownership of the property.

But there's a fundamental dispute beyond that, which is if it's not owned, literally owned, by either side, what sort of obligation was created by the lease with regard to the prepaid rent, and what are the parties' rights under the Bankruptcy Code with respect it?

It seems to me that that's --

MR. GREGER: Well --

THE COURT: -- that's barely touched upon in the

briefing and isn't really addressed in the complaint at all.

MR. GREGER: If I'm understanding Your Honor correctly, you -- your concern is that the -- the rights of the parties with respect to prepaid rent under state law was not adequately addressed?

THE COURT: No, no. No, again, Buckner says state law controls unless the Bankruptcy Code says otherwise. The Bankruptcy Codes says a lot, both in the Code and in the caselaw about set off and recoupment in making --

MR. GREGER: Right.

THE COURT: -- a distinction between pre and post, et cetera.

In state law cases, it really doesn't matter what sort of characterization is paid -- placed on prepaid rent as long as it's not determined to be the tenant's property because the money's owed to the landlord in some way, shape, or form. Although, I suppose there may be cases out there, although no one's really addressed in assist to, you know, prepaid rent for the last three months of the lease, the debtor -- the debtor breaches the lease well before then, and the landlord actually mitigates, then where does the prepaid rent go? You know that -- that would be --

MR. GREGER: Actually, Your Honor, we have -- we have addressed that.

THE COURT: Well --

MR. GREGER: We've asked the Wagner decision from the Supreme Court in Florida, where the Florida Supreme Court said that the prepaid rent is earned. It -- it doesn't get reduced.

THE COURT: Earned when? Pre or post?

MR. GREGER: Earned upon payment.

THE COURT: Well, that's pre then.

MR. GREGER: So, that -- and --

THE COURT: So, yeah, I think, again, it's -- it's -- to me, it would be premature to decide that issue, the recoupment, or setoff issue, in this context where I have a motion to dismiss a complaint that seeks turnover, which I think you correctly state -- although, again, I'll hear the Debtors' counsel on this -- requires that the interest not be in dispute, the interest and the property to be turned over. And I think it's clearly in dispute. I would say so, even under Pennsylvania law.

But beyond that, where it may be a debt as opposed to an interest, I think we're really getting pretty really far afield from the complaint and the motion to dismiss. I mean, I guess it's conceivable to me that I could, on a motion to dismiss, not only decide that it's not the Debtors' property, but that, in fact, it's the defendant's property. But this -- this record doesn't really let me decide that. I think -- I think it's just -- I think it --

I mean, I think there should be a separate, if the Debtors want to bring it, action as to declaratory judgment as to what this asset is, this money is. Is it a debt, is it a property interest? And if it's a property interest, whose? If it's a debt, how it subject to either setoff or recoupment? How is it characterized pre and post, for example?

MR. GREGER: Yeah, and Your Honor --

THE COURT: Post-petition.

MR. GREGER: Your Honor, we touched on the issue of setoff.

THE COURT: I know you touched on it --

MR. GREGER: But again --

THE COURT: -- but the -- but in this context, it's pretty -- pretty remote touching.

MR. GREGER: But -- but I -- let me speak to setoff then very -- very quickly.

Obviously, 553 allows setoff, and Your Honor correct points out that in the context of setoff under 553, you're out the recoupment. Setoff requires mutuality, which the courts have interpreted to mean both the underlying debt owed by the counterparty to the debtor and the claim that the counterparty has against the debtor, both arise in prepetition period.

We submit, Your Honor, that's easily established

here because the courts -- for example, we cited the Braniff decision in our reply brief. The courts look at the transactional basis for the genesis of when a claim arises. This is not when the obligation actually comes due. It doesn't matter if it's matured or contingent. What matters is when the underlying action was -- that gave rise -- the transaction that gave rise to the claim was entered into. If it was prepetition, then it's a prepetition obligation.

And here, there's just simply no debate. We entered into a lease prepetition. The prepaid rent was paid prepetition. All the underlying actions that give rise to a potential right of repayment to the extent the Debtors have one at all under state law relate to those prepetition actions, and thus, by -- by definition, any rights the Debtors have are prepetition.

We know on the flip side of this transaction, Congress has been eminently clear in 365(g) of the Code that the landlords' rights of -- to the payment of damages from the rejection of the lease are a prepetition claim. And in fact, courts have now fairly and almost universally found that it's appropriate for a landlord to set off its rejection damage claim against a security deposit, which is delivered prepetition on the basis that that security deposit is in effect a prepetition debt that the landlord owns -- owns -- owes the tenant. Sorry.

THE COURT: All right. But this isn't a security deposit.

MR. GREGER: Right. Which means that the Debtor (sic) doesn't even have a claim here. There is no debt owed by the landlord, but assuming that it -- it is a contingent debt, it clearly is a prepetition debt that the Debtor has. It had a contingent right to payment under the terms of the lease in the event there was a contingency or a default.

But let's assume that it -- somehow, the Debtors' still able to assert it, it's still a prepetition claim because the underlying prepaid rent was paid prepetition and the lease was entered into prepetition.

Then we look at the landlords' rights to damages as a result of the rejection of the lease. Your Honor, we filed proofs of claim here under -- following the rejection of the lease. The claims were filed timely. The landlord asserts more than $11 million -- well, approximately $11 million in combined damages. The Debtors haven't even reject -- objected to those claims. Those claims are deemed allowed under 502 of the Code.

So, purposes of set off as we stand here today, Your Honor, I disagree with -- with Your Honor. There is no basis to assume anything other than there's a complete set off because the Debtors have not and will not object to the 52 -- 502(b)(6) damages because we know why, Your Honor.

They're subject to Rule 11. If they want to make that objection, they better have a reasonable basis to do it, and of course, there is none, which is why they haven't challenged the claim here.

That claim is deemed allowed. There's no basis for the Debtor to argue otherwise, unless and until it brings an appropriate qualified objection to that claim. So, as we stand here today, there is -- after we go through all this, a complete setoff of everything.

And then, Your Honor, I do want to see --

THE COURT: Well, do you -- what is -- what is your client's administrative expense claim?

MR. GREGER: So, Your Honor, remember the -- the Debtor took the position that the base rent was satisfied, that it could recoup effectively, the base rent obligations for months 6 through 12, against the prepaid rent. Assuming the Debtor is correct -- and so far, we haven't challenged the Debtor -- the only additional administrative obligations the Debtor had were the additional rent under the lease.

And the claim that we filed was $145,000 combined for the two leases of unpaid post-petition 365(d)(3) additional rent obligations that accrued. Since the time we filed that claim, Your Honor, we actually believe that that number's big -- larger. But that's not relevant to today's hearing.

And then the final issue here, Your Honor, and -- and this is -- is interesting because the Second Circuit in -- in In re Stoltz, actually addressed with the effective rejection is, you know, and I -- I think it compliments what the Supreme Court did in (indiscernible) --

THE COURT: I'm not focusing really on the effective rejection. I'm focusing on what the prepaid rent should be applied to. I mean, it's -- it says in the parties' agreement, it should be applied to specific months.

MR. GREGER: That's correct.

THE COURT: So --

MR. GREGER: And rejection didn't terminate the Debtor's obligation to pay those months.

THE COURT: Well, if those months --

MR. GREGER: It --

THE COURT: -- are administrative, then you're saying it would be applied to those?

MR. GREGER: That's what the -- with respect to the administrative months, that's the position the Debtor took. And that's what they did.

THE COURT: But -- but -- I know. Are you disagreeing with that?

MR. GREGER: Your Honor, we believe what's good for the goose is good for the gander. And the Debtor gets it with respect to months 6 through 12, then the same

recoupment analysis applies with respect to months 13 through 18. It's the same -- same issue on the flip side. We're literally taking the prepaid rent for each month and -- and recouping it against their obligation to pay the rent for that corresponding month, which they breached.

It is -- is the closest case for recoupment that I can think of. Not only it -- does it arise under a single integrated transaction -- well, actually two because there's two separate leases and two different prepayments of prepaid rent, but it's the same corresponding obligations that are being recouped. Month 13 of prepaid rent against month 13 of -- of the rent that they breached by rejecting the lease, and we go up, 14 to 14, 15 to 15, 16 to 16.

And it is -- it is literally the closest case, and best case, for recoupment I can think of. And of course, when recoupment applies then there is no claim. It literally extinguishes the claim altogether. So, there's nothing for the Debtor to pursue here.

The same analysis would apply with respect to the common law rule with respect to prepaid rent. Once it's paid, it only become not refundable as provided in the lease. And the provisions in the lease for refund are not applicable here, so the Debtor doesn't even have a right to -- to get paid anything under state law. But assuming it did, it's recouped and it's done. It's -- there's not --

there's no claim here.

And that's why we submit, Your Honor, particularly in the context of a 542 action, there's no basis for the Debtor to stand in front of this Court and say, this is an undisputed amount that's owed to us, we hereby invoke the core jurisdiction of this Court, and have the right to pursue this core claim. There's just no basis for it.

THE COURT: Okay.

MR. GREGER: And it needs to be dismissed.

THE COURT: All right. Why don't I hear from the Debtors?

MS. CROZIER: Good morning, Your Honor, and may it please the Court? Jennifer Crozier, Weil, Gotshal & Manges for the Debtors on the Debtors' opposition to the landlord's motion to dismiss.

THE COURT: Morning.

MS. CROZIER: Good morning, Your Honor.

The Debtors acknowledge that the -- that if there is a legitimate dispute concerning title through the subject property, then this action was not properly brought as a turnover proceeding. However, for the reasons I'll discuss in a moment, Your Honor, the Debtors submit that there is no legitimate dispute concerning whom owns these unused prepaid rent it owns, and that accordingly, this property falls clearly within Your Honor's turnover power.

Now, the landlord's relied very heavily on this argument that caselaw determines the nature and extent of a debtor's interest in property, and that Florida and Pennsylvania law, which govern the Imeson and Hanover leases, respectively, provide that landlords are entitled to overturn of the prepaid rent, or rather to retain the prepaid rent upon a tenant's default.

But as the landlords themselves admit, the parties to a contract can contract around state law with respect to prepaid rent, and that's exactly what the parties did here. So, even if Florida and Pennsylvania law do provide that landlords are entitled to retain prepaid rent on a tenant default, and as Your Honor, yourself recognized, that's not at all here, with respect to Pennsylvania law. But even if they do, Sections 36 and 10 of the leases provide otherwise.

First, Your Honor, to Section 36. The landlords have argued that they earned the prepaid rent at the moment they received it. But the language in Section 36 belies this argument. Section 36 provides in pertinent part, and I quote, "Provided Sears has not been in default under this lease, the landlord shall apply the prepaid rent, Sears's obligation to pay monthly fixed rent as and when due". So, in the ordinary course, that is when the Debtors were not in default -- in the ordinary course, the Debtors could only apply the prepaid rent, is Sears's obligation to pay monthly

fixed rent as and when due, which the Debtors submit means that under the leases, the landlords didn't earn the prepaid rent until the moment it became due.

Now, the cases the landlords themselves --

THE COURT: But what -- what about the opening provisor there? I mean, Sears is in default because it rejected the leases.

MS. CROZIER: Right. And I'm going to address that in a moment, Your Honor because Section 10 of the leases address the landlord's obligation with respect to the prepaid rent upon Sears's default.

But if I may for a moment address Section 36 very briefly and then I'll turn to Section 10?

THE COURT: Okay.

MS. CROZIER: The -- the landlords cite Burns Trading against Welborn, it's a Tenth Circuit case, 1936. Rather old, but in that case, the Tenth Circuit considered a provision very like the one that's in here, which among other things, provided for the application of a prepayment for the last years' rent, "when due". And the court in that case concluded, "It is clear from these provisions that title to the deposit was to remain in the" lessee "until it should be properly applied on rental or retained as liquidated damages on termination of the lease." And that's what we're arguing here. Until the moment that monthly

fixed rent obligation became due, (indiscernible) to the unused prepaid rent amount, (indiscernible) to the prepaid rent remained a retainer.

Now, in that case -- in the Burns Trading case, the landlord was entitled to retain the prepaid rent precisely because there was an express provision in the contract that said upon termination, you get it as liquidated damages. But here, the leases don't have that. In fact, they say just the opposite.

Now, I'll turn to -- to Section 10 now, which addresses the remedies to which the landlords are entitled upon Sears's default. And if Your Honor looks to Section 10(a), (indiscernible) (iii), the -- the very last clause of that provision, it says, "In no event shall Sears be liable for any consequential, special, punitive, or other similar damages."

Now, again, Section 10 enumerates the remedies to which the landlords are entitled upon Sears's default, and not one of those remedies allows the landlords to retain the prepaid rent. But again, what's most important here, is what this provision does say, and it does say they don't get consequential, special, punitive, or other similar damages.

Now, should the landlords retain the unused prepaid rent amounts, that would constitute an award of consequential, special, punitive, or other similar damages

because these amounts are over and above the landlords' rejection damages claim. The landlords --

THE COURT: Why?

MS. CROZIER: Well, the landlords' rejection damages claim, Your Honor, that asserts their direct damages, up to the statutory cap set forth in Section 502(b)(6) of the Code.

To be clear, the landlords have not considered the unused prepaid rent amount in their calculation of their rejection damages. They themselves treat these amounts as separate and apart from their direct damages.

THE COURT: Is that right, Mr. Greger?

MS. CROZIER: But in --

THE COURT: I don't -- I don't think that's -- I mean, look, I'm assuming they filed a breach claim for the remaining amount -- the remaining term of the lease.

MR. GREGER: Your Honor, our claim is for the damages that stem from the rejection of the lease capped by 502(b)(6). There's no --

THE COURT: But --

MR. GREGER: -- provision of our claim -- our state law damages far exceed 502(b)(6), and counsel's represent --

THE COURT: I know. I understand. But to get to the 502(b)(6) cap, you first do the calculation of your --

MR. GREGER: State law damages.

THE COURT: -- breached damages.

MR. GREGER: That's correct.

THE COURT: And I'm assuming that would include -- maybe I'm wrong. I'm assuming that would include these months of the lease.

MR. GREGER: It would, but our position -- and I guess this is an issue for the Court to decide later on -- our position is that it doesn't get reduced against the 502(b)(6) cap. And maybe counsel's suggesting that the prepaid rent should be treated akin to a security deposit and reduce the cap. It's a distinction without a difference because it -- it's not going to affect our rights to the prepaid rent.

THE COURT: Well, I don't know. I mean, I -- but I -- but I -- it would seem to me that -- I could certainly envision scenarios where a landlord's rejection claim under 502(b)(6), just for amounts that would have been paid under the lease if the lease hadn't been rejected, you know, i.e., breached, would not be consequential, special, punitive, or other similar damages, but would just be lease breach damages, which Subsection 3 of Article 10, gives the landlord the right to assert.

MR. GREGER: Correct.

THE COURT: But if -- if the landlord wants to

treat the lease as terminated, 3(c) says, the "worth at the time of the award of the amount by which the unpaid rent for the balance of the term after the term of the award exceeds the amount of unpaid rent." And then five -- little Roman (v) says, "If the landlord does not elect to terminate the lease, it can enforce all of the landlord's rights and remedies under this lease, including the right to recover all rent as it becomes due."

Now, of course here, the -- I don't know what you've done as far as terminating or not terminating, but the rejection creates a prepetition claim, in --

MR. GREGER: Right.

THE COURT: -- any event. So --

MR. GREGER: That's correct.

THE COURT: -- I'm just not sure that the analogy to the Tenth Circuit case works here because here, we're talking about a breach claim that arguably, at least -- unless the parties stipulate that this isn't the case -- is greater than consequential, special -- you know, it's just the claims for breach as opposed to consequential, special, punitive, or other similar damages.

MS. CROZIER: Understood, Your Honor. And again, the Debtors submit, at the very least, there is a legitimate -- at the very least, if there is a legitimate dispute here, then the -- you know, to the extent there is a legitimate

dispute, that the Court should dismiss the complaint without prejudice --

THE COURT: Okay. All right.

MS. CROZIER: -- for the Debtors to seek relief by --

THE COURT: I mean, I didn't know -- for example -- the facts don't really -- because it's a motion to dismiss -- it's not clear to me whether the landlords re-let the space. I don't whether that's the case. I mean, it -- warehouses are actually -- because some places are premium because they're being used by Amazon and people like that, or to house multiple computers that are mining Bitcoin. So, I -- you know, it's -- I don't -- I don't have those facts that this point.

MR. GREGER: Your Honor, we -- what we do know is that the claim hasn't been objected to, so it's --

THE COURT: Well --

MR. GREGER: -- deemed allowed.

THE COURT: -- there's -- there's no -- yeah. But that's -- that's -- that -- there's no deadline to -- I think --

MR. GREGER: Understood. But as we stand here today, there is no dispute that our claim is valid and deemed allowed. That's what 502 provides.

THE COURT: All right.

MS. CROZIER: Your Honor, it's like -- if I may, as you yourself recognize, you know, whether -- whether the landlords have mitigated is not in the record. It's not before Your Honor. We don't know whether they've mitigated. We don't know whether they've gotten more rent, the same amount. So -- you know, these set off and recoupment issues really aren't appropriate for adjudication at this stage on a -- on a motion to dismiss.

THE COURT: Okay.

MS. CROZIER: If I may just address one more issue? You know, our position has been that -- that in order for setoff and recoupment to apply, the property or (indiscernible), there must be a debt, and the Debtors' position is that the unused prepaid rent amounts do not constitute a debt. And in fact, Mr. Greger himself said that in his argument a moment ago. He said there is no debt owed by the landlord and, you know, to the extent -- again, there's been a lot of argument about setoff and recoupment. We don't believe it, you know, adjudicable (sic) at a motion to dismiss. So, our position has been that no debt exists here; rather, the landlords are hold the Debtors' property and such setoff and recoupment would not apply.

THE COURT: Well, I guess the -- the dispute there though is that the landlord is saying it's not a debt because it's -- it's the landlords' property, or at a

minimum, it's subject to recoupment, which is just a running account as opposed to a debt. So, I think that -- I mean, I agree there's a dispute over that. But -- but I don't think they conceded that -- I mean, far from it, that, in fact, not only is there no debt, but the property is the Debtors'.

MS. CROZIER: Understood. They have not conceded that, Your Honor.

THE COURT: Okay. Okay. All right. Anything else from anyone?

All right. I -- I have a motion before me by the defendants in this adversary proceeding, Sears Holdings Corporation, et al., v. 1055 Hanover Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007) and one Imeson, I-M-E-S-O-N, Park Boulevard, LLC, to dismiss the sole count in the complaint pursuant to Federal Rule of Civil Procedure 12(b)(6), as incorporated by Bankruptcy Rule 7012.

The standard for a motion to dismiss is well recognized in the caselaw as set forth in the statute itself, or the rule itself, as well as the Supreme Court's decisions, Ashcroft v. Iqbal, 556 U.S. 662 (2009), and Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007). The courts must accept as true all well pleaded factual allegations and draw reasonable inferences from them. But the court should not credit merely conclusory allegations or legal conclusions couched as factual allegations, i.e.,

allegations that simply mirror the underlying elements of the cause of action without setting forth the factual basis for the cause of action. And of course, the complaint must state a claim that is above the speculative level over the plausible claim for relief.

Plausibility is not really the issue here. The issue is whether the facts as alleged in the complaint set forth a basis for the underlying cause of action, which is a asserted right to turnover of prepaid monthly rent under the respective leases, which have the same term as to prepaid rent in each lease, Paragraph 36.

Section 542(a) of the Bankruptcy Code requires "that an entity in possession, custody, or control, during the case, of property that the trustee may use, sell, or lease under Section 363 of this title, or that the debtor may exempt under Section 522 of this title shall deliver to the trustee," or the debtor in possession, "and account for, such property or the value of such property, unless such property is of inconsequential value or benefit to the estate."

Clearly here, the complaint relies upon the terms of the two leases, which are effectively incorporated into the complaint. So, of course I can consider the leases as part of my consideration of the underlying motion to dismiss.

Based on its plain terms, Bankruptcy Code Section 542(a), requires the trustee or debtor in possession to establish three things. One, the property's in the possession, custody, or control of another entity. Two, the property can be used in accordance with the provision of Section 363 of the Bankruptcy Code. And three, the property has more than inconsequential value to the debtor's estate. In re Khan, K-H-A-N, 2014 WL4956676 at p. 22 (Bankr. EDNY, September 30, 2014.

There's really no issue here as to the value of this property. It's in excess of a million dollars under each lease, and the property's clearly -- or was at least clearly in the possession, custody, or control of the respective landlords, post-petition, and thus demanded by the Debtors and they have refused to provide it. The issue as to whether the property would, in fact, be property of the Debtors' estate and could be used in accordance with Section 363 of the Bankruptcy Code, the Debtors acknowledge that where there is a bona fide dispute or during the dispute, as to the estate's interest in the property sought to be turned over, a turnover claim does not lie. Instead, the Debtor must establish its right in the property, at which point it can assert turnover or some other right to relief based on the results of that resolution of the dispute.

Even if the Debtors had not recognized, it's a well-established proposition. See, for example, In re Lexington Healthcare Group, Inc., 363 B.R. 713, 716-17 (Bankr.D.Del. 2007), and the cases cited therein.

On the flip side, in a motion to dismiss context, the defendants here are not seeking, or they could not be seeking a determination of their entitlement to the prepaid rent, but are rather simply seeking to dismiss the complaint.

Of course, the dispute might be so obvious that I could make a ruling on that basis. But I am not prepared on the record before me to do more than dismiss the complaint without prejudice, thereby preserving the Debtors' rights to argue either through a separate proceeding that they, in fact, have an enforceable interest in the prepaid rent, or alternatively that if they don't have such an interest, it is subject to application as they assert -- or as they would assert in such proceeding to the landlords' claims in this case, with any excess to be returned to the estate.

The Debtors contend that on the plain language of the lease the parties agreed that under the facts as they exist today, the prepaid rent is either refundable to the Debtors, or actually for turnover purposes, the property of the Debtors, not subject to any claim of the landlords. I conclude, based on my reading of the lease that there's at

least a bona fide dispute as to that contention.

Paragraph 36 of each lease states, "On the effective date, Sears shall provide landlord with an amount equal to" then it states the amount -- it's different for each lease --- "i.e., 12 months of monthly fixed rent otherwise due during months 7 through 18 of the term", and then "(the defined term, prepaid rent) as prepaid due under this lease for months 7 through 18 of the term." The next sentence states, "Provided Sears is not then in default under this lease beyond any applicable notice or cure period, landlord shall apply the prepaid rent to Sears's obligation to pay monthly fixed rent as and when due until the entire amount of the prepaid rent has been exhausted, provided however, if this lease is terminated due to a landlord default," casually -- "casualty condemnation or the early termination rights described in Section 3 above, then landlord shall promptly return the unapplied portion of the prepaid rent to Sears".

It's clear from that provision that the parties did agree specifically when the landlord shall return the prepaid rent to Sears, and the complaint does not assert that any of those things have, in fact, occurred. There is no other provision of the lease that says what happens to the prepaid rent other than in those specific circumstances, which don't apply on the face of the complaint.

The landlord asserts that one would incorporate applicable state law to fill that gap. And it appears to me that the law in Florida is clear that under those circumstances where the parties have not agreed to the express return of the prepaid rent to the tenant, the landlord, at a minimum, can apply it to amounts owing under the lease. Those cases are cited at some length in the motion itself, and they include Wagner v. Rice, 97 So.2d, 267, 271 (1957) and Casino Amusement Co. v. Ocean Beach Amusement Co., 101 F. 59 (1931). Florida law, as I said, is relatively clear on this issue as to the gap-filling provisions of state and common law.

Pennsylvania law is less clear. But at least for purposes of the motion to dismiss, one can confer -- infer that there's at least a bona fide dispute that the courts in Pennsylvania that applying their state's law would follow, what appears to be the majority view on this issue, which is unless the parties have expressly provided otherwise, the landlord can use prepaid rent upon a default under the lease.

What is not clear to me, however, is how such a right, if established, on the part of a landlord, would be affected by the parties' agreements and the operations of Section 365, 502(b)(6) and 502(g) -- I'm sorry. Yeah, 502(g) and 365(g) of the Bankruptcy Code, as well as the

Bankruptcy Code setoff provision, Section 553, as well the Bankruptcy Court's interpretation of the recoupment doctrine and its applicability here.

Before turning to those issues, I do want to discuss two of the cases cited, really against the majority view in the caselaw that's cited by the movants. Those two cases cited by the Debtors, both come in a bankruptcy context, and they argue that in a bankruptcy context the rule under the majority common law as to the landlord's right to prepaid rent, unless the parties clearly provide otherwise, is somehow modified and create an actual property interest in the prepaid rent in the Debtors estate.

The first one, Marshall v. Shipment Elevator Co. (In re Marshall), 240 B.R. 302 (Bankr. S.D. Ill. 1999) is clearly distinguishable. There, the Court found a constructive trust in favor of the debtor with respect to the equivalent of prepaid rent. In that case, it was prepaid storage charges. However, in that case, the grain storage facility or operator -- shipment, acknowledged that "the storage arrangement was one which the debtors were free to terminate at any time whereupon shipment would have the obligation to refund the unused portion of the money." It was under that circumstance where the defendant acknowledged that it would have that obligation that the court found a constructive trust in favor of the debtor.

The other case relied upon by the debtors, In re Orangebrook Concessions, Inc., 47 B.R. 858 (Bankr. S.D. Fla. 1985), really addresses a different issue. There, the debtor was not looking to assert an interest to the exclusion of the interest of the landlord in prepaid rent when a lease had terminated or been rejected under Section 365 of the Bankruptcy Code.

Instead, the landlord was looking to retain prepaid rent as adequate protection, relying on lien rights under Section 553 of the Bankruptcy Code. The court determined that in those circumstances the landlord did not have a lien, or under 553 of the Bankruptcy Code, a statutory right equivalent to a lien on the prepaid rent that will require it to be adequately protected. In part, it did so in way that's frankly puzzling to me, notwithstanding that the lease said that the prepaid rent would be held that a security deposit under Paragraph 24 of the parties' lease.

The case really did not deal at all with the fact pattern where a lease has been rejected and the landlord is holding prepaid rent in that circumstance. And therefore, it did not address how that prepaid rent could be applied, if at all, by the landlord.

Here, I could take judicial notice of the fact that the two leases have been rejected under Section 365 of

the Bankruptcy Code, which clearly gives rise under the Code itself and is acknowledged by the Supreme Court recently in the Mission Product Co. v. Tempnology (sic) case, 139 S.Ct. 1652 (2019), that gives rise to a prepetition claim and a breach, but does not, in the words of the Supreme Court, "vaporize" the lease as if it doesn't exist, and therefore, eliminate that claim.

That leaves, however, open what the prepaid rent amount could be applied to, and I believe in a motion to dismiss context that issue on this record should not be decided. I don't have the claim in front of me. I don't know what its components are. The Debtors' have not sought to object to the claim. And until there is an objection that's deemed allowed, but that doesn't mean that I can determine on a motion to dismiss that, in fact, the claim is allowed, and, more importantly, how this money can be applied to it. That is a proper subject to mitigation should the Debtors choose to bring it, or alternatively, if the landlord would want to make a motion for relief from the stay to apply the money to its claim, in each -- in each -- with respect to each claim.

So, I will grant the motion and enter an order dismissing the complaint, which again, seeks only a turnover claim. But I will do so without prejudice since -- if the Debtor establishes a right in the property with respect to

either of the two leases, in a separate complaint, the turnover cause of action would be appropriate to put in that complaint as well.

And separately, because I believe it's neither the subject of the complaint, all of the Debtors' rights with respect to setoff and recoupment, and the ability to object to claims that have been filed should be fully preserved, as would be the respective landlords' rights.

So, I'll ask counsel for the landlords to submit an order to that effect. You don't need to formally settle that order on the Debtors, but you should copy their counsel on the email to chambers so that they can confirm that it's consistent with my ruling. And it's probably a good idea just to run it by them briefly before you send it.

We don't have to do anything more than refer to my bench ruling. You don't have to summarize or quote it, but simply say, for the reasons stated in the Court's bench ruling at the hearing, the motion should be granted as provided in the -- in the order.

So, are there any questions on that?

MR. GREGER: No, Your Honor. Thank you for your time.

MS. CROZIER: No --

THE COURT: Okay.

MS. CROZIER: No. Thank you, Your Honor.

THE COURT: Thank you.

MS. MARCUS: Thank you, Your Honor.

THE COURT: Okay.

MS. MARCUS: Going back to the agenda, we have one more matter on for today. Before we get to that though, Your Honor, if I may, one sort of housekeeping matter? As you may recall, at the April 27th hearing, we had oral argument regarding the Debtors' motion to compel, transform to pay additional funds related to the foreign cash.

THE COURT: Yes.

MS. MARCUS: And at that time, you -- you issued a preliminary ruling and gave Transform time to file additional pleadings, which they did --

THE COURT: Right.

MS. MARCUS: -- and the Debtors filed their additional pleadings. I was just wondering if you could give us some insight and -- as to when we'll know when whether your order has become final?

THE COURT: I haven't -- I haven't had a chance to go through them, frankly. I was waiting for them to get -- to get filed. They were emailed to chambers I think at the end of last week. And I'll -- I'll give you a link if I think a further ruling is warranted at the next omnibus date. But I may enter the order before then if I believe that those pleadings don't change my mind from the

preliminary ruling that I gave the parties, in which case I'll reach out to the Debtors to submit the order.

MS. MARCUS: All right. Thank you, Your Honor.

THE COURT: Okay.

MS. MARCUS: So, the last -- the last matter on the calendar is another -- is another motion to dismiss. It's Matter No. 11 on the agenda, and I believe Ms. Casteel will be handling that. I'm -- well, I guess it's not the Debtors' motion. It's the other side's motion.

THE COURT: All right. Right. It's the motion of Winning, W-I-N-N-I-N-G, Resources Limited to dismiss the complaint in Kmart Holding Corp. and Sears Roebuck and Co. v. Winning Resources Limited on the basis of Federal Rule of Civil Procedure 12(b)(5), incorporated by Bankruptcy Rule 7012, i.e., insufficient service of process.

And on this one, I have read the pleadings through the reply filed by the movant on the 21st -- yeah, on the 21st.

MR. BANICH: Good afternoon.

MS. CASTEEL: Your Honor, sorry. This is Kara Casteel. I just wanted to clarify that it's the Katten Law Firm responding to this motion, so not me.

THE COURT: Okay. All right. So, who is it going to be? It's going to be Mr. Wander for the movant and who for the -- for the plaintiff?

MR. BANICH: That would be me, Your Honor. Terence Banich from Katten.

THE COURT: Okay. Very well. Thank you.

MR. BANICH: Thank you.

THE COURT: All right. I -- I guess I have a basic question here. When did the plaintiff start to serve the defendant under the Hague Convention? When did that process start?

MR. BANICH: Yes, I'm sorry. I wasn't sure if you were done speaking, Your Honor. Terence Banich from Katten. It is my understanding that the process with the -- for service under the Hague Convention began on or about February 12th of this year.

THE COURT: And the complaint was filed when?

MR. BANICH: I believe it was in October of 2020. I can get you the exact date, if I could just shift over to the docket on this. One second.

MR. WANDER: Your Honor, July 7, 2020.

MR. BANICH: Ah, July 7th. Okay. It was in an earlier (indiscernible).

THE COURT: Okay. And when was the answer filed?

MR. BANICH: We have that -- our objection --

THE COURT: I mean, I -- I --

MR. BANICH: October 12th, 2020.

THE COURT: I guess that was the -- that was the

October date you probably had in mind.

MR. BANICH: Yes, Your Honor.

THE COURT: Okay. All right. So, was there any discussion after the answer was filed and before the process under the Hague Convention was started regarding service between the plaintiff and the defendant, i.e., an extension of the time or discussion about accepting service otherwise, or anything like that?

MR. BANICH: Your Honor, I guess I should probably address that first. In our objection to the motion, on page 1, we recite various interactions we had with defense counsel --

THE COURT: Right.

MR. BANICH: -- on this matter. In particular, the stipulations to extend time reference therein with regard to discovery, and that was after the answer was filed. So, this would have been in November of 2020. And then following that in December, we entered into another stipulation -- and again, though that was with regard to discovery.

THE COURT: Right.

MR. BANICH: And then it was only six months after the answer, defendant the answer, and following the two stipulations I just referenced, that the defendant filed this motion.

THE COURT: Right. So --

MR. BANICH: I'm not -- sure.

THE COURT: -- were there any discussions about service during that period?

MR. BANICH: Oh, yes. We did have -- Mr. Wander and my firm, we did have some discussions wherein Mr. Wander indicated that there was a problem with service, and we had some discussions that -- about that issue that may be more appropriately characterized as settlement discussions. So, I'm not sure of what extent I want to get into them. But we did discuss settlement; rather, I should say, service at that time.

THE COURT: Well, I -- I think, again, 408 just goes to settlement discussions not being disclosed as for the evidence of the bona fides of the claims. I'm just focusing here on whether there was any -- on the one hand, suggestion that -- coming from the defendant that the plaintiff could delay service or hold off on service, or effect service some other way. Or alternatively, any statements from the defendant that, you know, I told you that you haven't served this properly, you need to serve it properly, we're pursuing this. One or the other? Did any of that --

MR. BANICH: That --

THE COURT: Either of those things occur?

MR. BANICH: Assuming that question's directed at me --

THE COURT: Yeah.

MR. BANICH: -- and I'll take that liberty, Your Honor. At -- Mr. Wander, in our discussions, did indicate that they were taking the service issue seriously. I don't believe that they ever indicated that we could serve them in another way or that they would agree to accept service.

Though, I will say that in the context of those discussions, we -- the plaintiffs did try to get past the issue of service in the context of getting to the point where we could negotiate an agreed resolution of the merits. But I cannot say that Mr. Wander agreed to accept service.

THE COURT: Okay. Okay. All right.

So, this is the odd motion to dismiss where the Plaintiff actually has the burden to show a proper service, although the inability to satisfy that burden on the facts is fairly light so, I actually directed my questions to Mr. Banich for that reason. And maybe given the extensive and fairly clear briefing on the parties, I should ask some more pointed questions on this point.

One of the points that the reply makes is that -- well, it acknowledges that the Plaintiff raises two grounds for service being sufficient. The first being that I can apply the exception for a foreign defendant in Rule 4(m),

and/or the good cause exception on top of the exception to the exception.

The reply states that's well and all good, but there's no factual support for it offered up, no declaration or affidavit or emails or anything to that effect. The motion also states that under Rule 4(f)(3) three, alternative service on Mr. Wander will be sufficient, given his participation in the case, the stipulations that you've referred to, etc.

But the reply makes the argument that that really needs to be done, again, proactively by the Plaintiff and can't be asserted in a reply to a motion to dismiss, but rather should be in a separate motion. I guess I'd like to have your response to both of those points.

MR. BANICH: Yes, Your Honor. I believe, with -- when it comes -- let's -- if I could take the -- take up the second point first.

THE COURT: Sure.

MR. BANICH: Since we're fresh off of it. Yeah. So, there are a number of points, although I do -- I would like to take the liberty to interpose what I consider to be a threshold issue is whether this motion is timely or not.

THE COURT: Well, we'll come back to that.

MR. BANICH: And I don't know if we'll come back -- okay. I know -- don't want to come -- lose sight of that,

but --

THE COURT: Right.

MR. BANICH: But focusing on the matter of the -- I believe this is what Mr. Wander refers to as a procedural defect with the 4(f)(3) argument.

THE COURT: Right.

MR. BANICH: Specifically that it requires a motion. It is somewhat ironic that that argument appears in the reply brief, because just a few pages before, the Defendant complained that the debtors were elevating form over substance and this is perhaps a fairly good example of elevating form over substance, but nonetheless, I would suggest that the plain language Rule 4(f) resolves this issue because it does not, by its plain terms, require that alternative service only be granted upon a motion or after notice at a hearing or words to that effect that appear in several other rules, where that type of formality is required.

Rather, subsection three simply says the Court can approve alternative service, “as the Court orders”. It doesn’t say how the Court gets to actually render such an order, but I would suggest there’s a motion before the Court now to dismiss and part of the order that the Court may enter could in -- authorize an alternative form of service and the rule would be satisfied.

THE COURT: Okay.

MR. BANICH: So, I -- that's sort of, I think the plain language of the rule there; where is the requirement that it be by motion? We just can't do it without Your Honor's authority. I think that's the takeaway from 4(f)(3), and that makes sense.

THE COURT: So, could I interrupt you on that point?

MR. BANICH: Yeah.

THE COURT: Because that is --

MR. BANICH: Of course.

THE COURT: -- what the rule says. Mr. Wander, what would the debtors request in their -- actually it's an it. What would the Plaintiff's request in their objection to the motion deprive you of by having it heard now as opposed to by a separate motion under Rule 4(f)(3)? I mean, do I have all the facts in front of me? Is there something that you think that the record needs to be developed on?

MR. WANDER: Well, I don't think it can get to Rule 4(f), because there's no showing that they made any attempt to properly serve. So, I would not stand on -- necessarily on the formality of the not serving a notice of motion. Because, you know, Your Honor, we're here. I made the point, but the point really -- the issue really is that they didn't try at all to serve. Not at all. And if I can

address the undisputed facts --

THE COURT: Well no, I guess -- so, it's really not a -- I'm just drawing your -- we'll get to those other points, I'm just looking at the procedural point. So, it's really less a procedural point than you're relying on 7004(m), really.

MR. WANDER: Yeah, because I don't want this to be adjourned and then they file a cross motion, so I'm --

THE COURT: Yeah, but what I'm saying is, you really -- your focus on (f)(3) is to take me to (F)(4), I mean 4(m), time before service. Right?

MR. WANDER: Yes.

THE COURT: Okay. All right. So then, Mr. Banich, on the first point that I raised, the evidentiary burden that you have?

MR. BANICH: Right. I would say there's two real responses to that. I think we return to Rule 4(m) in the advisory committee notes that added subsection (m) in 1993, and that the point here is is that the Defendant's motion seems to assume that the Plaintiffs are subject to a good cause requirement under Rule 4(m), but if, as we pointed out in our objection and as the advisory committee notes from 1993 state, and I'm going to quote, it's not that long, it says 4(m), "explicitly provides that the Court shall allow additional time if there is good cause for Plaintiff's

failure to effect service in the prescribed 120 days, and authorizes the Court to relieve a Plaintiff of the consequences of an application of this subdivision even if there is no good cause shown."

So, I don't want to lose sight, this is -- that's from the advisory committee notes. So, I don't want to lose sight of the premise might be in error; that there is this good cause requirement that's inescapable. I think the Court has more latitude than that. So, I don't want the record to reflect that I'm agreeing that we're bound by that showing.

Nonetheless, as we pointed out, and I don't think I need to belabor the point about the effect of COVID and the timing here. I mean, the complaint was filed in July, and if we're not talking about good cause and how to evidence that, and the answer was filed in October. I mean, that was the height of the pandemic.

There are plenty of cases, and we cited a few of them, that talk about, and the Court can take judicial notice of the disruption to every aspect of American life, or life on this planet, frankly, because of COVID, and so kind of not sending someone into China to try to effect service of process at that time seems to be somewhat more understandable when considered in light of what was going on, particularly last summer.

But, to get to the more specific point about how to evidence it, we're happy to submit some form of declaration from the process server that we've engaged for this purpose, if that would be of use or be necessary for that point.

THE COURT: Okay. All right. Why don't we go, then to the point, Mr. Banich, that you alluded to, which is this motion to dismiss was made after the answer.

MR. BANICH: Yes, Sir.

THE COURT: And you contend that we shouldn't be hearing on a motion to dismiss basis.

MR. BANICH: Yes.

THE COURT: It's not a waiver point, right, because the answer itself --

MR. BANICH: That's correct.

THE COURT: -- raised the defense of improper service.

MR. BANICH: Yes, sir, and you're quite right, it's -- and I think the case that we cited from the Northern District of Illinois actually, there's a block quote in our objection, makes that precise point. There's a distinction between being able to file a Rule 12(b) motion to try to get dismissal for insufficient service, that's over here, and on the other side you have a waiver of a defense from a Rule 8 perspective, which is a totally different issue. We are not

contending, for the record, that the Defendant here waived the affirmative defense of its insufficient service.

I mean it -- the Defense appears in the answer it's obvious they have it, the only issue is whether this motion is untimely, and the -- this is one of those situations where the rule itself actually is pretty clear and addresses this, and it makes it clear you cannot file one of these types of Rule 12(b) motions after filing an answer, and I think the flashpoint between the parties on this is that, and concededly, there are lower court decisions that go both ways on this issue.

We have argued that there is the Second Circuit's decision in Beacon Enterprises actually is controlling, and kind of points the way with regard to which line of cases the Court should follow here. And I have a number of things to say about that, and I've heard Your Honor say you read everything, so.

THE COURT: No, go ahead.

MR. BANICH: I --

THE COURT: It's fine.

MR. BANICH: Okay. What I mean to do is simply just go through the points raised in the reply, so I don't more or less repeat stuff you've already read. Let's start with the Beacon point, if I may. Mr. Wanders' main response to this is that it's -- that the -- what the Second Circuit

said here about, you know, in connection with this issue was dicta. But, I would say that -- in an attempt to elevate form over substance, that's why I mentioned that point earlier. I would argue that identifying a case that's probable circuit precedent is controlling is not elevating form over substance, it's what we do and how we make arguments and carry out our duty of candor.

And by the way, it's not -- there's really no analysis in the reply about why Beacon is dicta. Dicta as I'm sure Your Honor knows, is whether the statement in the the opinion we're citing is necessary for the decision of the case. Second Cir -- I can cite cases along the way for things I'm going to say, Your Honor, do you want me to do that or only if you say where does that proposition come from? I'm happy to do it either way.

THE COURT: Whatever you're more comfortable with.

MR. BANICH: All right, well, I'll include cites for the record, and if it gets -- if you feel it's too pedantic, please let me know.

THE COURT: Okay.

MR. BANICH: Anyway, it's a common principle that dicta is, whether or not the resolute -- the statement was necessary for the resolution of the case, and that's, for example, Morrison v. Eminence Partners, 714 F.App'x 14 at 1617, (2d Cir. 2017).

Now, what was going on in Beacon Enterprises is necessary to understand why it wasn't dicta. And so, very briefly, what was going on there? The Defendant in that case contested personal jurisdiction and, like the Defendant here, she answered but then later moved to dismiss under Rule 12(b)(2), which deals with lack of personal jurisdiction.

Later in the proceedings, the District Court converted her motion to dismiss to a motion for summary judgment without any notice to anyone and then proceeded to deny her motion for summary judgement as it had then become, and found that the court had jurisdiction over her and then, also that she'd lost on the merits.

The Second Circuit reversed that decision, and without getting into the merits, which have literally nothing to do with what we're talking about today, the court held that it was error among other things to convert her dismissal motion to one for summary judgement without notice, including as to the personal jurisdiction issue.

And then, bringing us to the point of why I'm talking about this decision, the court concluded that, and I'm going to quote here, "because untimeliness of the motion to dismiss contributed to the procedural confusion at the hearing below, Beacon, the Plaintiff, should receive opportunities for discovery on the jurisdictional issue and

be allowed to present evidence at a formal hearing on the motion to dismiss for lack of jurisdiction". That's 715 F.2d 757, 768.

So, I would say the untimeliness of the motion and its -- and what happened to it was relevant to how the Court issued the remand, what the lower Court was to do on remand.

THE COURT: But, I guess --

MR. BANICH: So -- yeah, sorry.

THE COURT: Here, I mean I'll ask you the same question I asked Mr. Wander. Is there any real prejudice, at this point, by treating this as a 12(c) motion?

MR. BANICH: Well, there are cases that say it's not legally appropriate to convert a Rule 12(b)(5) motion to a Rule 12(c) motion. So, I guess the -- it would be a legal problem, rather than one of prejudice, I would say.

THE COURT: Right, but the record isn't -- unlike in Beacon, it doesn't seem like -- I mean, everyone has notice, what's -- what Mr. Wander is arguing here.

MR. BANICH: Yes.

THE COURT: I think the facts -- I don't know what needs to be developed further, if anything. Is there anything that needs to be developed further?

MR. BANICH: Not factually, if that's what Your Honor's referring to.

THE COURT: Right.

MR. BANICH: Other than the matter of the evidence of -- if we're going to discuss when the debtors tried to commence Hague service, so for (indiscernible).

THE COURT: Right.

MR. BANICH: Other than the good cause -- evidence of good cause, on the other matters I would say no, it's on -- some -- as to insufficient service there is no factual record that needs to be developed, other than if we're going to talk about good cause, or its absence.

So, the -- I don't know if weu drifted into the 12(c) argument, but I have a couple of -- if you want -- if Your Honor wants --

THE COURT: Well, let me ask Mr. Wander, what else could I do besides 12(c) here to get around the limitation on bringing a motion to dismiss after there's been an answer?

MR. WANDER: Well, first of all for the record, if I may just, Your Honor -- David Wander of Davidoff Hutcher and Citron, counsel for the (indiscernible).

Judge, so, very interesting issue, and I don't think Beacon is a bar, at least the Second Circuit didn't think it was a bar, and we've cited Agency Rent A Car System v. Grand Rent A Car. That was a 1996 Second Circuit decision and that described courts in the Circuit and others that have allowed a rule 12(b) motion to dismiss in cases

with analogous procedural patterns after the filing of an answer preserving the affirmative defense on which the Rule 12(b) motion was raised.

Then you have a whole slew of District Court decisions that have allowed the 12(b) motion to dismiss after the filing of an answer. We even cited one case where they did it under Rule 12(c) and the District Court, I believe it was, criticized them -- the Defendant for not moving under 12(b). So, I don't believe there's any bar to this Court ruling under 12(b), but another way to deal with that conundrum as we cited, and as Your Honor was just alluding to is under 12(c), and the standard's the same. The standard's the same. But, let me tell you --

THE COURT: Although it's on the pleadings, which is a different -- I mean this isn't really on the pleadings, right, this is based on service.

MR. WANDER: Yeah, and there's --

THE COURT: So, it's really -- to me, it really just goes to the case law that says you can do this or not do it after an answer's been filed, under 12(b).

MR. WANDER: But we -- since everyone agrees the Defendant preserved the issue, no one's arguing waiver, we've got to be able to bring it before Your Honor in some fashion, and I submit better sooner than later, why go through discovery and anything else in the case --

THE COURT: Well, the only issue would be whether there is -- there needs to be this --

MR. WANDER: Go ahead.

THE COURT: The only issue would be whether there needs to be further discovery on this issue. On the service issue.

MR. WANDER: Can I address that?

THE COURT: Yeah.

MR. WANDER: So, we pointed out in our papers, in our reply, that there's no evidence to support the Plaintiff's burden. None. And --

THE COURT: What that -- but that begs the question, if they want to -- arguably that's because they want to have a ruling first on whether you could do this under 12(b) after an answer.

MR. WANDER: Judge, if they want to tell Your Honor what actually happened, you asked counsel for plain -- for the Plaintiff whether any discussions, I'm the one who had the discussions if Your Honor would like to hear what exactly happened I'll -- I'm happy to tell you what happened and what they --

THE COURT: Well, again, I guess Mr. Banich, let me go back to how -- what prejudice would there be to the Plaintiff here if I ruled on these papers, on this issue? Is there additional evidence that you would want to

introduce, now that you would know that I might be ruling on a 12(b)(5) basis regarding the Plaintiff's attempts to serve, the limitations on service, anything like that?

MR. BANICH: I would answer that as follows. I would say, if the scope of Your Honor's ruling included the matter of good cause, the 4(m) issue, if it included, for example, the 4(f)(3) arguments we made about what counsel has done, even though I think that contacts with the case and with us, even though I think the docket would evidence that, then I think we would want to make sure that Your Honor had the benefit of knowing when we, for example, commence service under the Hague Convention and things of that nature, but I -- do I think we're going to take discovery on anything? I don't believe so, Your Honor.

THE COURT: But you would want to submit an affidavit and Mr. Wander could cross-examine the affiant if he wanted to?

MR. BANICH: The only -- I imagine the only matter addressed by the affiant, other than who the affiant is and what they do was when they put the papers out for service, as it were. I don't think the affidavit really addresses anything else.

THE COURT: Well, they could be willing to talk to someone and they said it's going to be really hard, I'm just speculating --

MR. BANICH: Oh.

THE COURT: -- about this. I'm sure this is going to be really hard to do in Hong Kong, etc. because they're locked down or whatever, I don't know if that happens, but that -- conceivably that could be --

MR. BANICH: Right.

THE COURT: -- something that you'd want to submit.

MR. BANICH: Yeah, I -- that's right. If we were having a discussion about good faith attempts and the difficulties of effecting service in the Far East at this time, then yes, I would want to expand it to include that. I'm just trying to figure out what would we be considering the whole group of arguments that have been made here today or just some lesser, smaller subset? And it sounds like everything. So.

THE COURT: Okay. All right.

MR. BANICH: Did you -- would you -- would Your Honor want me to address the 12(c) argument that --

THE COURT: I think this is really best --

MR. BANICH: No?

THE COURT: -- addressed under 12(b), if you're going to address it at all, just by the plain terms in 12(c).

MR. BANICH: All right.

THE COURT: This isn't really judgement on the pleadings.

MR. BANICH: Right.

THE COURT: It really isn't.

MR. BANICH: Right, I agree with that. Right. So, I think we're on the same page there. So, the issue, I don't know if you've moved past the Beacon Enterprises issue or not, but we're not a -- the debtors aren't on an island on this issue, as we pointed out in our objection, it was Judge Torres followed Beacon in this Moore v. Shahine decision, 2019 WL 948349, (S.D.N.Y. Feb. 27, 2019). So, if district judges are relatively recently treating Beacon as -- and this point Beacon as a holding, it's not unreasonable for us to suggest to Your Honor that it's also a holding.

THE COURT: Right.

MR. BANICH: And if that's the case, then this motion is untimely and we don't really have to go any further. So, with that I guess I'll take Your Honor's suggestion about where you'd like -- what points you'd like me to address next.

THE COURT: Well, I mean I think you've addressed all your points, really. The first one is the timeliness issue.

MR. BANICH: Mm hmm.

THE COURT: And the meaning of Beacon. And the

second and third are the 4(f)(3) and 4(m) issues.

MR. BANICH: There are a few more points I like that came up in the reply on 4(f)(3) that I'd like to address, if that's all right.

THE COURT: Okay.

MR. BANICH: That I -- we didn't have occasion to discuss before.

THE COURT: Okay.

MR. BANICH: Okay. Now, there's a couple of points. We've just -- we've discussed the alleged procedural effect, I'll skip that one. The main argument here is -- the main point in both the motion and the reply is that the debtors were somehow obligated to at least attempt service first before trying to under -- and that's under 4(f)(1), before trying to invoke 4(f)(3) for authority to affect a form of alternate service, and that's -- that is at least incorrect under a line of cases that we have argued.

But before we even get to that issue -- well, actually I'll come back to that. That's fine. So, the -- as we pointed out in our objection, 4(f)(3) is an option that has equal dignity with the options under subsections (1) and (2) of 4(f).

So, three is an option just as equally as one under Hague service as an option, and that's what Judge

Buchwald noted in a decision we call Zhang v. Valaris, 2021 WL 982460, *3, (S.D.N.Y. Mar. 16, 2021). And I would add to that that nothing in the text, syntax or structure of Rule 4(f) requires a party to attempt Hague service, that is attempt subsection (1) before seeking alternate service under subsection (3).

Now, obviously, there's some cannons to statutory interpretation we could go through, but suffice it to say Federal Rules is interpreted for its plain language just like a statute is and, obviously, that means it's inappropriate to graft things onto the rule that aren't there. And there's a lot of cases out there that do that. And Mr. Wanders cited and talked about a lot of them. However, I think that absent a controlling decision here, which is apparently the case, the safer course and better course is to do a -- follow the plain language of the text of the rule.

And that is that the three subsections of Rule 4(f), Your Honor, are phrased in the disjunctive. There's an "or" that follows subsection (2) leading into subsection (3), and when that happens, statutes written in the disjunctive create, "separate and distinct alternatives". And that's in re: Modansky, M-O-D-A-N-S-K-Y 159 B.R. 139, 143, (Bankr. S.D.N.Y. 1993).

So that is to say, if that's the case the

disjunctive phrase -- phraseology of Rule 4(f) compels the conclusion that service under subsection three is a separate and distinct alternative than Hague service under subsection (1).

THE COURT: Although --

MR. BANICH: Yeah.

THE COURT: Doesn't China's opting out of any other alternative besides the Hague Convention mean that (f)(3) wouldn't apply because service on Mr. Wander, where he's not active as the agent for service or otherwise said he would accept it is prohibited by international agreement.

MR. BANICH: That's obviously an excellent question and the first time you encounter this issue you would not be faulted for thinking that. But the cases that hold, that service on a domestic representative such as a domestic lawyer who has been -- who has shown to have some contact with a foreign Defendant, the reason it doesn't offend the international agreement, the Hague Convention, is because the Hague Convention does not regulate service domestically in the United States. And that is why it -- the analysis the Courts go through. So, it is -- China only gets to talk about service within China.

But this is a form of service within the United States. So, that concern -- that is why the two pre-requisites for 4(f)(3) service, which I would point out, Mr.

Wander doesn't address at all in his motion or reply, so the point I would suggest to you is tacitly admitted that we've satisfied the elements for 4(f)(3) that's why it doesn't offend an international agreement because we're talking about serving the Defendant via an agent within the United States.

THE COURT: Okay.

MR. BANICH: And that -- I mean, that's the analysis these courts use, including Judge Leisure in the Madu, Edozie & Madu, P.C. case cited in our objection when Judge Leisure wrote that service of process under 403 is neither a last resort nor extraordinary relief. It's merely one means, amongst several, which enable service of process under an international Defendant.

I think that our -- although there's plenty of cases that the defense talk about, that go on for many pages discussing this case and that case that went the other way on this issue, I would suggest though, that the way I've -- the case is holding that there is no threshold showing required, that we at least tried Hague service first. It's the better course to follow, because it's more -- it is more in line with the plain language and syntax of the rule. Of Rule 4(f), I should say.

So, that is -- I think that is the -- all I wanted to say in addition on the 4(f)(3) point. Happy to take any

questions Your Honor has.

THE COURT: No, I guess I have a question for Mr. Wander, which is, do you have a response to the other -- to the -- you've made -- and I've reviewed and considered your respense -- response on the timing point and whether I should allow (f)(3), given the timing of the attempted serve under the Hague Convention. Do you -- I think it's true, you haven't really addressed the other elements of (f)(3). Due process and -- is there a problem there?

MR. WANDER: Well Judge, I think we addressed the fact that, in order to get to (f)(3), you have to first at least attempt to comply with the Hague Convention, and to a certain extent there should be a stop from making this argument --

THE COURT: Actually, you don't really need to. I mean, one of the very cases you cited summarizes the case law that says you don't. There's no pre-requisite.

MR. WANDER: Judge, they have a --

THE COURT: In that case, that's the Halverson case, they hadn't ever tried, even at the time of the motion. So --

MR. WANDER: Judge --

THE COURT: -- they were -- they fell into the "whimsically seeking an order of alternative service".

MR. WANDER: So, we had a proceed -- we have a

procedures motion. And the procedures motion says in sum and substance, Plaintiffs will follow the Hague Convention and they've never said why they didn't. There's no issue that they have the right address. There's no issue that the Defendant did not try and evade service. And every case basically that I've looked at where the Court granted some alternative means is because there was a basis for them. There was a reason why they couldn't try serving.

Here, they made no effort, even to comply with their own procedures motion. They never --

THE COURT: Well -- I -- the procedures order doesn't require service under the Hague Convention.

MR. WANDER: Judge, but --

THE COURT: And the motion just alerts people in the context of telling them that they may not actually, in terms of the timing issues for the settlement dealing with claims and claims objections and administrative expenses, this may -- as I read it, the reference to compliance with the Hague Convention is one to alert people who ask to make a choice as to how they elect to have their administrative expense treated, that it may take a while for their claim to be resolved because it takes a long time, often, to serve under the Hague Convention. I didn't see it as a requirement that it be done.

MR. WANDER: Well, it's interesting your -- as

Your Honor pointed out, what they put in the motion and have been -- this is just the fifth one, what they've put in the motion they didn't track in the order. Now, my client hadn't been served at that time, I couldn't really respond to it, but the motion made it clear to the Court, it made it clear to everyone that they intended to serve under whatever international law required the service. If they simply could -- if they can ignore it, simply ignore it, and then after a Defendant makes the motion to dismiss, then they ask Your Honor for relief that they never needed, because they could have followed the Hague Convention.

THE COURT: Right.

MR. WANDER: They could have --

THE COURT: But that's different than saying the debtors in a motion said that they would only follow the Hague Convention.

MR. WANDER: The procedures motion, I think it was paragraph five, made it very clear that that's how they were going to do it. And here, they didn't even try. My client did not evade service. The address they have is not incorrect.

THE COURT: Well they -- but they have tried. They were outside 100 -- they were outside 90 days, but they have initiated that service.

MR. WANDER: They weren't. After I had

discussions with them and asked them why they didn't follow their own procedures motion --

THE COURT: Well, but -- look. You're not going to convince me that the procedures motion set a specific way as the only way to serve foreign Defendants here. The reference in that motion to service under applicable conventions, like the Hague Convention, I took to mean to make it clear to parties that it might take a long time for adversary proceedings, upon which recovery parties were going to be relying to get paid, now that -- to get off the road. This wasn't --

MR. WANDER: Well --

THE COURT: -- a matter where the money was going to be coming in with regard to foreign Defendants quickly, because it often takes hundreds of days to serve it. That was the context of that motion.

MR. WANDER: Right, and also, by the time they got around to filing the summons and complaint, it was something like nine months after the confirmation hearing, and when they say that well, what about COVID, they knew about COVID. In the procedures motion that we're dealing with in August, I believe, they didn't change what they may have (indiscernible) instead to Your Honor in the first procedures motion. They could have come to Your Honor and said COVID. We need alternate means of service. It's

difficult to get into China or any --

THE COURT: The procedures motion doesn't limit how you serve someone. It just doesn't.

MR. WANDER: Correct. The law does. The statute does.

THE COURT: Well all right, so you should stop referring to the procedures motions that somehow it either constitutes a waiver or some negative circumstance. I think -- I understand your other points. What we're talking about here, I believe, is a -- I'm just doing the math, here. The process to serve under the Hague Convention started February 2.

MR. BANICH: I'm sorry, Your Honor. February 12th.

THE COURT: 12th.

MR. BANICH: Just so we're clear.

THE COURT: So, you'd be in mid-May, basically, with the 90 days to initiate the process. And no I -- excuse me. I believe I have the wrong date. You'd be in September. The beginning of September because the complaint was filed in, did you say July --

MR. BANICH: July.

THE COURT: -- 6th? Or June 7th? Was it July?

MR. BANICH: It was July, Your Honor.

THE COURT: July. So, it'd be in October. July

6th, roughly would be the 90 days. So, you're talking about a four-month delay. The answer was filed October 12th and I don't know if there were any discussion before then. I mean, the answer was filed well after I think the time to file an answer, so were there discussions before then, about your -- we'll extend your time to answer?

MR. WANDER: Well first of all, Your Honor.

MR. BANICH: Yes. Yes, Your Honor, I'm sorry. I didn't mean to interrupt, but yes, Mr. Wander and -- did contact us and we evidently entered into a stipulation on October 7th to extend time to answer or respond to the complaint. Yes. And that's docket number four in the adversary proceeding, Your Honor.

THE COURT: Okay.

MR. BANICH: Sir, I didn't mean to interrupt. I'm sorry.

THE COURT: So, anyway Mr. Wander, are you -- you were saying that the time limit just wasn't met here?

MR. WANDER: What I'm saying is they deliberately didn't meet the time. There was no excuse. They simply chose to serve by mail.

THE COURT: But the case law doesn't require an excuse. There are two standards to apply, and the likely standard, the one that should apply under 4(m) is a standard that says if you really delay a lot, then you should go to

the good cause standard.

MR. WANDER: And here they waited more than --

THE COURT: Well, when I say a lot, the cases are talking about two years.

MR. WANDER: But I think a lot of the cases are talking about less. They filed the com -- the summons and complaint in July and they didn't make any attempt until the following February, after we made the motion. After I told them, we're making a motion to dismiss because you haven't given any reason why you didn't try and properly serve. So, after then, we say we're going to file the motion to dismiss. At that point in time I submit, it's too late. Otherwise we've --

THE COURT: Do you have a case that says that? I dealt with this issue a week or so ago, and looked at it pretty carefully, and I don't think the case law actually says that. It doesn't have a drop-dead when someone makes a motion to dismiss like that.

MR. WANDER: Correct, there is no specific date, I know we cited the Veon case, there are cases -- there is no specific date. It doesn't say -- it basically says if you want to ask for something alternative relief, then you need --

THE COURT: That's fair, I'm focusing on 4(m) at this point.

MR. WANDER: Well, I submit that under the facts of this case, you can't just wait 200 days. I'm not saying 199 days is okay, but 200 isn't. But where you have a situation where the Plaintiff simply decides not to follow the rules that we're supposed to be guided by, then that's -- they should not be given additional time. Otherwise why have the rule?

THE COURT: Well, it would be 120 days after the 90-day deadline.

MR. WANDER: Right. After the 90-day deadline when they should have asked Your Honor for some alternative means, if they thought they were going to have difficulty. Here they just didn't try.

THE COURT: No, but again, I'm just focus -- I'm not focusing on (f)(3).

MR. WANDER: Right, so there's no --

THE COURT: I'm focusing on m, 4(m). And the cases dealing with 4(m) don't really -- particularly in a situation like this where there was an extension of the time to answer and it appears, at least from what you both have told me, that the discussions about the failure to serve took place in October, November at the earliest, that what we're talking about here is a meaningful delay. I just -- to me it's not consistent with -- at least the case law, which really references either still not having made an

attempt to serve, I'm not talking about the 4(m) case law. Or, not having done so for like, two years, five years, one was five years. I mean, they're a long period.

MR. WANDER: Well, Judge, we have a case here with hundreds of adversary proceedings being filed. It's not like this got lost in the sauce. They made a deliberate, strategic decision not to follow the rules.

THE COURT: The rules don't -- the rules are not expressed. 4(m) actually says the 90-days doesn't apply under 4(m). When it's a service on a foreign party.

MR. WANDER: Almost every case that deals with giving additional time, the Plaintiff has given some cause. Something. I haven't seen a decision where they did absolutely nothing and even contradicted what they had said they would do. They haven't even met the lowest threshold of seeking the relief. It was not until more than 200 days after they originally filed, multiple discussions with them asking them why didn't they follow the proper procedure, and then they said, we're going to be filing a motion to dismiss. At that point I submit, it's too late, Your Honor.

THE COURT: You -- I know you've submitted that, but you haven't given me any cases to that effect, and I have plenty on the other side, so I guess I -- to me this fits under 4(m).

MR. WANDER: Well, again, I don't know of a case

where the Plaintiff deliberately didn't try and serve the way they were supposed to, engaged in discussions --

THE COURT: There are plenty of cases like that, where they just sent a letter or an email. There are lots of cases like that.

MR. WANDER: Judge, we've had the -- I know the procedures motion was not engrafted in the order. I know there's no specific deadline by which time it's too late, but if you allow the late service in this case, then the procedures that we follow in these cases become meaningless. I mean, they could have taken a default against my client, gotten a default judgement, because they were serving by mail. Had my client not contacted me, they probably would have gotten a default judgement.

THE COURT: No, they wouldn't because they would have had to have submitted their certificate of service. And I wouldn't have granted it.

MR. WANDER: Well, Judge, I submit under the facts of this case, where they did nothing. They haven't submitted a declaration, anything.

THE COURT: But we have the facts. I -- we have the facts. I don't think there's anything more -- it's acknowledged that they didn't commence the effort to serve until February 12th. Is that -- Mr. Banich, is that when you actually served it, put it in the mail, or did you hire

a process server before then?

MR. BANICH: I'd have to -- there's some complexities associated with Hague service, I don't want to characterize it the wrong way, but I -- it's my understanding that the -- if you're the service company, they consider the process to have been started on their end on February 12th.

THE COURT: But you -- I'm assuming you reached out to them beforehand? I don't --

MR. BANICH: Oh, yes. That's correct. We had to find the right person who does this sort of work and that part of the --

THE COURT: That's all part -- I actually think, frankly, it's likely that I will grant -- I will deny the motion saying that the standard under Rule 4(m) has been satisfied here. But, I do think that the Plaintiff here is entitled, because this motion was made after a answer was filed, the Plaintiff here is entitled to submit the facts to justify either relief under 4(m) or 4(f)(3). And I'd like to have that record before deciding the motion.

But, I can tell you that given the back and forth with counsel, including the extensions of the time to answer and three stipulations and the like, that I don't think that, at least from what I've heard thus far, the Plaintiff runs afoul of the Court-imposed process for fixing a

deadline to serve a foreign Defendant under Rule 4(m).

There's a very good discussion of those rules, a recent one by Judge Engelmeyer and On re Astor Chocolate Corp. v Elite Gold, 2020 U.S. LEXIS 78862, (S.D.N.Y. May 5, 2020) that I think is a very good summary of the law on this issue. It doesn't deal with (f)(3). I'll note that the (f)(3) cases give a considerable amount of discretion to the Judge, separate and apart, and I think frankly, both analyses come down to whether the Court feels that the Plaintiff, under the specific facts, has been unduly dilatory in serving. Not on excuses regarding service, which would be the good cause standard, a separate, extra right that this Circuit gives Plaintiffs under 4(m), but that is not -- I would think even necessary to get into here given the interpretation of 4(m) in the Circuit.

I will note that I think that there are cases that say that the Plaintiff must have begun within the 90-day period to try to serve, or else they fall into the good cause only exception, like Bozel, which you refer to. But, they rely upon a case that really doesn't stand for that proposition, which is the Honeywell case. And then, I believe they mis-cited that case by -- one was federal practice, Section 4.52(d)(4). In fact, the case law in that case, the Honeywell case, the Plaintiff never tried to serve, ever.

Which is a far cry from saying that you have to try to serve within the 90 days. So, it's fact-based and in fact the cases that -- except for the ones that I think misread Honeywell, and they're the distinct minority, that don't allow service outside of that -- either the 120 days or now the 90 days, have focused on a really lengthy period, with no excuse whatsoever, no pre -- and plenty of prejudice to the other side, which I don't think is the case here.

So, I don't think we need to get into the exercise of discretion beyond good cause either, which is yet another way out that the Courts have given Plaintiffs, which takes into account, among other things, the anal -- the applicability of the statute of limitations and the like.

But, we don't have a full factual record here. I'd -- I rarely have one. But, I think at this point, in -- to me the choice is either 4(m), and the Hague Convention, or (f)(3) -- 4(f)(3) and service on Mr. Wander, and I'm -- it seems to me that if -- at this point, the Plaintiff's going to rely on the Hague Convention, then the motion really should be denied. I think I would need a better record under (f)(3) than I have now, if the Plaintiff also wants to say that the drawback of a -- the service on Mr. Wander through (f)(3).

MR. BANICH: Okay.

THE COURT: But I'm assuming if we -- if there's a

record of settlement discussions, if there's -- there are three stipulations, October, November, and December, I just clearly Mr. Wanders' been in contact with the client, he couldn't engage in settlement discussions without that. I mean, otherwise you wouldn't be engaging in settlement discussions because you wouldn't have authority.

MR. WANDER: There weren't any.

THE COURT: What?

MR. WANDER: There weren't any settlement -- they were not settlement....

THE COURT: Well, that's the say -- that's why I would want a record, to see whether there were such a things. But if there were, than (f)(3) might well apply. But I don't have that record.

MR. BANICH: Is the -- may I ask a clarification question? Is -- a moment ago I thought I heard Your Honor say the -- to the effect that the choices between 4(m) and the Hague Convention on the one hand, or 4(f)(3) in service on --

THE COURT: Right.

MR. BANICH: -- Mr. Wander on the other, and I believe Your Honor went on to say that if the Plaintiff were to stand on Hague service the motion should be denied?

THE COURT: With one exception, which is Mr. Wander --

MR. BANICH: Okay.

THE COURT: -- do you dispute that it -- that at least at the latest, the process was started on February 12th, 2021? Or is that also not established?

MR. WANDER: I have no reason to dispute it. I don't know.

THE COURT: Okay. So, I think to just answer your question, Mr. Banich, I think I need evidence on that. I can't grant the -- I can't deny the motion based on this record.

MR. BANICH: All right.

THE COURT: I'm not going to grant it either, so --

MR. BANICH: Okay.

THE COURT: -- we can adjourn it to the next round of this. I'll see the affidavits, but until I do that everything -- if that's the date or even if it's earlier when you began the process based on the case law that I cited to you all, I will deny that motion under 4(m).

MR. BANICH: Very good. I appreciate that very much.

THE COURT: And again, if you want to still seek alternative basis under (f)(3), then you do obviously need to get that record before me as well, for that adjourned hearing.

MR. BANICH: I understand, Your Honor. Thank you.

THE COURT: Okay. All right. Thank you.

MR. WANDER: Thank you, Judge.

THE COURT: Okay.

MR. BANICH: Thank you, Your Honor.

CLERK: And then I think that brings us to the conclusion of this rather lengthy hearing.

THE COURT: Right.

CLERK: Thank you for your time.

THE COURT: Okay, very well, thank you all.

CLERK: Thank you.

MR. BANICH: Thank you.

(Whereupon these proceedings were concluded at 3:29 PM)

C E R T I F I C A T I O N

I, Sonya Ledanski Hyde, certified that the foregoing transcript is a true and accurate record of the proceedings.

Sonya Ledanski Hyde

Veritext Legal Solutions

330 Old Country Road

Suite 300

Mineola, NY 11501

Date: May 25, 2021